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CHILD CARE: THE EMERGING INSURANCE CRISIS

mf117 ORIGINAL

HEARINGS

BEFORE THE

SELECT COMMITTEE ON CHILDREN, YOUTH, AND FAMILIES HOUSE OF REPRESENTATIVES

NINETY-NINTH CONGRESS

FIRST SESSION

HEARINGS HELD IN WASHINGTON, DC, ON
JULY 18 AND JULY 30, 1985

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CHILD CARE: THE EMERGING INSURANCE CRISIS

THURSDAY, JULY 18, 1985

House of Representatives,
Select Committee on Children, Youth, and Families,
Washington, DC.

The committee met, pursuant to notice, at 9:35 a.m., in room 2257, Rayburn House Office Building, Hon. George Miller presiding.

Members present: Representatives Miller, Rowland, Wheat, Coats, Johnson, Monson, Smith, and Gejdenson.

Staff present: Ann Rosewater, deputy staff director; Jill Kagan, professional staff; Anne Wynne, minority professional staff; Carol Statuto, minority professional staff; and Joan Godley, committee clerk.

Chairman **Miller**. The Select Committee on Children, Youth and Families has convened this hearing to look into recent reports of dramatically reduced availability of liability insurance for providers of child care services.

The committee is deeply concerned about the impact of this crisis on millions of American families and their children, for whom child care is an essential service.

Child care centers, family day care homes, Head Start Programs, and resource and referral agencies report that their liability policies are not being renewed, that premiums have become prohibitive, that coverage for child care abuse claims is unavailable and that policies are being cancelled with little or no notification.

As recently as this week, we have heard reports of highly credentialed family day care providers who not only have had their liability coverage cancelled midterm, but who have been told their homeowner's coverage is at risk for nonrenewal.

In my own district the situation reached the point that many providers threatened to strike. In nearly half of the States, including California, the problem is complicated by the requirement that child care providers carry liability insurance in order to be licensed.

But in order to secure insurance, they are being told they must first be licensed. This is a classic catch-22 case.

The select committee has completed a year-long investigation into the escalating demand for child care services. That report, which we issued, which was signed by all the members of the committee, recognized that child care is a reality for millions of American families, and that the supply of reasonably priced, reliable, and accessible care is woefully inadequate.

Now, we find that the existing facilities may be forced to shut down, to reduce the quality of their services, or to operate illegally without coverage due to the lack of liability insurance.

Should an impasse be reached where insurance is not available to child care providers, the ramifications for working American families could be catastrophic.

For millions of families child care is an absolute necessity to the economic well-being of the family. If insured child care is not available, these families will be forced to make a decision between their economic livelihood and the well-being of their children. This is a problem that affects millions of families in all of our congressional districts. Clearly, the failure to provide coverage is unacceptable.

Today we will review the best available information on this problem. In the committee's tradition, we have sought testimony from those who have experienced the problem directly, the child care providers and those in the insurance industry who have been involved in these policy changes.

Unfortunately, each of the many representatives of insurance and underwriting companies, as well as State insurance commissioners whom we have invited, declined that invitation.

I very much regret the industry's refusal to provide witnesses, but I will, with the approval of the members of this committee, move to leave the record open for an additional week in order to receive any testimony which the industry might provide for our consideration.

I would like to recognize, at this time, Congressman Gejdenson, who has joined the committee for the purposes of this morning's hearing. Sam?

[Opening statement of Chairman George Miller follows:]

OPENING STATEMENT OF HON. GEORGE MILLER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA, AND CHAIRMAN, SELECT COMMITTEE ON CHILDREN, YOUTH, AND FAMILIES, JULY 18, 1985

The Select Committee on Children, Youth, and Families has convened this hearing to look into recent reports of dramatically reduced availability of liability insurance for providers of child care services.

The committee is deeply concerned about the impact of this crisis on millions of American families and their children, for whom child care is an essential service.

Child care centers, family day care homes, Head Start programs, and resource and referral agencies report that their liability policies are not being renewed, that premiums have become prohibitive, that coverage for child abuse claims is unavailable, and that policies are being cancelled with little or no notification. As recently as this week, we have heard reports of highly credentialed family day care providers who not only have had their liability coverage cancelled midterm, but who have been told their homeowner's coverage is at risk of nonrenewal. In my own district, the situation reached the point that many providers threatened to strike.

In nearly half the States, including California, the problem is complicated by the requirement that child care providers carry liability insurance in order to be licensed. But in order to secure insurance, they are being told, they must first be licensed. This is a classic "Catch 22".

The select committee has completed a year-long investigation into the escalating demand for child care services. That report, signed by all the members of the committee, recognized that child care is a reality for millions of American families, and that the supply of reasonably priced, reliable, and accessible care is woefully inadequate.

Now we find that existing facilities may be forced to shut down, to reduce the quality of their services, or to operate illegally without coverage due to the lack of liability insurance.

Today, we are seeking a clearer picture of what is happening and why. In the committee's tradition, we have sought testimony from those who have experienced the problem directly, the child care providers, and from those in the insurance industry who have been involved in these policy changes.

Unfortunately, each of the many representatives of insurance and underwriting companies, as well as State insurance commissioners, whom we invited declined the invitation. I very much regret the industry's refusal to provide witnesses, but I will, with the approval of the members of the committee, move to leave the record of this hearing open for an additional week beyond the regular period allowed, in order to receive any testimony which the industry might provide for our consideration.

I look forward to the testimony which will be presented and hope that it will begin to identify ways to solve this serious problem.

STATEMENT OF HON. SAM GEJDENSON, A MEMBER OF CONGRESS FROM THE STATE OF CONNECTICUT

Mr. GEJDENSON. Thank you, Mr. Chairman. I think it is important to note that Federal action can play a major role and I commend the chairman personally for his efforts 1½ years ago in adding training funds for day care workers. In my own State of Connecticut, that has resulted in a law that does provide for training and police checks for day care workers and thank you for allowing me to join you today. I commend the chairman for a swift action on this issue which is putting many day care centers in my district, and around the country, in jeopardy of being closed.

The need—the increasing need for day care centers is clear to all of us. Both here and in the Congress, when we find both parents in a family working and in our own districts. The short-sighted action taken in the early days of the Reagan administration which basically removed the Congress from much of its regulatory oversight in day care needs to be reversed.

It is the Federal Government that has virtually abdicated its oversight responsibility on the day care issue today. We find that this hearing is a necessary first step to make sure that citizens around the country, in many instances where both parents work, have available to them affordable day care services.

We commend the chairman for joining with us in asking for the report on trying to find the basic status around the country to see how much of an impact there is, what course of action we can take. I would hope that the insurance industry would be forthcoming in taking advantage of the chairman's generous offer to keep the record open; and, in additional hearings, that we would be able to hear from an industry that to a large degree is based in my State and plays a vital role in keeping these day care centers open.

Chairman MILLER. Thank you. Our first witness this morning will be Congressman Jim Florio, who has been a very good friend of the chairmen of this committee, but more importantly, a supporter of the issues and concerns this committee has tried to raise in the U.S. Congress.

Congressman Florio is a subcommittee chairman on the Commerce Committee. Jim, welcome to the committee.

[Prepared statement of Congressman Sam Gejdenson follows:]

PREPARED STATEMENT OF REPRESENTATIVE SAM GEJDENSON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CONNECTICUT

Mr. Chairman and Members of the Committee: Thank you for asking me to join you today to investigate the problems faced by day care providers in obtaining liability insurance. Swift reaction to this new and growing problem is essential if we are to avoid a national crisis for providers of day care and the millions of young families they serve.

As members of this committee are well aware, the need for quality, affordable daycare is increasing every day. Unfortunately, this need has not been accompanied by a comparable commitment of either Federal or State resources. Quite the contrary. In 1981 Congress drastically reduced day care funding and effectively ended any Federal involvement in the establishment of standards for day care programs receiving Federal funds.

Mr. Chairman, you have responded to the Nation's day care problems with an intelligent and well-crafted piece of legislation to address the major deficiencies in Federal day care policy. I was pleased to join you in cosponsoring that legislation. Part of the reason day care providers are facing the insurance problems they are today, I believe, is that the Federal Government has virtually abdicated its oversight responsibility in this area. By reinstating a day care earmark in the social services block grant, and by providing inducements for States to step up their child abuse prevention efforts, your bill would go a long way toward restoring to day care programs a set of national priorities.

Without those standards, day care centers from Connecticut to California already find themselves in the predicament of either not being able to get insurance coverage at all or being forced to pay three and four times their current premiums to maintain coverage. Apparently, reports of sexual abuse in several day care centers have led the insurance industry to now consider day care a high risk area. The accuracy of this assessment is as yet unclear. What is clear, though, is that day care providers will either have to raise their fees to compensate for increased insurance costs, or they will simply have to close their doors. What's more, the very people most likely to be forced to shut down are the in-home providers—those who provide the least expensive and most accessible form of day care around.

Mr. Chairman, you have joined me in asking the General Accounting Office to study the day care insurance issue. Today's hearing emphasizes that the problem is becoming more acute and is spreading at an alarming rate. It merits immediate congressional attention. Certainly there are no simple solutions for easing the day care insurance crunch. That is why I hope this hearing will be but the first step in a full-scale effort to examine this problem thoroughly and to address it in the swiftest, most effective way possible. I look forward to working toward that goal with you and members of the committee, Mr. Chairman, and again I thank you for asking me to join you today.

STATEMENT OF HON. JAMES J. FLORIO, A MEMBER OF CONGRESS FROM THE STATE OF NEW JERSEY

Mr. FLORIO. Thank you very much, Mr. Chairman and members of the committee. I do appreciate the opportunity to share with you briefly some thoughts, not only on the question of the emerging child care insurance crisis, but really the entire insurance crisis that we are experiencing in this Nation.

As chairman of the House subcommittee with jurisdiction over insurance, I believe it is very important that we monitor the activities of this very important industry, which is exempt from Federal regulation and is subject to very uneven regulation at the State level.

My concern is heightened, when as, in this case, the industry acts in a way that can impact negatively on the quality of American life.

The insurance industry appears to be going through a period of retrenchment, a reexamination of its own role in our economy and in our entire way of conducting business affairs. Insurance underwriters and carriers are refusing to offer coverage that is essential to the enforcement of many of our laws. The environmental laws are certainly a very important example. Toxic waste disposal coverage is not being made available.

The chairman is very active in the asbestos field and he knows that removal of asbestos is not an endeavor for which there is easy access to insurance coverage.

Nurse/midwives recently have been notified that their policies for medical malpractice insurance will not be renewed. And now the industry is sharply curtailing insurance for the providers of child care services, which, of course, is the subject of this hearing.

On that particular matter, the committee certainly knows that over half of all the mothers with infants and very young children in this country are now in the work force and their numbers are growing.

To these women and their families, the availability and the quality and affordability of child care is certainly critical and insurance plays an important role in determining those factors.

The insurance industry seems to want the best of many worlds. The industry wants to uphold coverage from all but what it determines to be the smallest and the most profitable of risks. At the same time it is waging a passionate fight to exclude banks and other financial institutions from entering the market to provide insurance.

Quite frankly, Mr. Chairman, to this point I have not been a very strong supporter of banking deregulation initiatives, which would obliterate the distinctions between insurance companies and investment brokerage houses and banks. I am starting to rethink through my commitment to the position that I have had over the last number of years.

I suppose as the ultimate fulfillment of our commitment to the competitive marketplace, that if someone is not going to provide the service and someone else says that they will provide the service, maybe we should think through whether we want to allow those other people to provide the service.

Last year, when we debated H.R. 100, which is a bill that would have prohibited sex discrimination in the providing of insurance, the insurance industry worked very hard to defeat that bill.

Right after the defeat, I heard from representatives of the banking industry, who said that if they had the opportunity to go into the insurance field as they would like to, they would be more than happy to provide for gender neutral insurance coverage.

Well, that is, of course, rhetoric. That is not a commitment, but it may very well be that we want to consider taking people up on more specific offers as to whether they are willing to go into this business.

In the upcoming months, I intend, and I see Mr. Coats is here, a member of my subcommittee, we intend to look into this question of the availability and affordability of insurance, particularly, focusing on environmental insurance but looking at the whole scope of insurance activities.

I am convinced that the findings of this select committee will aid us in the effort that we are going to become involved with in reviewing insurance action or inaction. I thank you for the opportunity to share some thoughts with you and I look forward to receiving the results of your deliberations.

[Prepared statement of Congressman James Florio follows:]

PREPARED STATEMENT OF HON. JAMES J. FLORIO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY

Chairman Miller and Members of this Select Committee, I greatly appreciate this opportunity to join you in this inquiry into the emerging child care insurance crisis.

As Chairman of the House Subcommittee with jurisdiction over insurance, I believe we must monitor the activities of the insurance industry—an industry which is exempt from federal regulation and subject to very uneven regulation at the state level.

My concern is heightened when, as in this case, the industry acts in ways that can impact negatively on the quality of American life.

The insurance industry appears to be undergoing a major phase of retrenchment. Insurance underwriters and carriers are refusing to offer coverages that are essential to the enforcement of our environmental laws. Nurse midwives were recently notified that their policies for medical malpractice insurance will not be renewed. And now the industry is sharply curtailing insurance for providers of child care services.

Over half of all mothers with infants and very young children in this country are now in the work force, and their numbers are growing. To these women and their families the availability of quality and affordable child care is critical.

The insurance industry seems to want the best of many worlds: the industry wants to withhold coverage from all but what it determines to be the smallest and most profitable risks. At the same time, it is waging a passionate fight to exclude banks and other financial institutions from entering the market.

In the upcoming months I intend to focus on several aspects of the availability of insurance issue.

I trust that the findings of this Select Committee will aid me in that effort.

Chairman **MILLER**. Well Jim, thank you very much for your interest. In our discussions it has become clear that should we find it necessary to address this problem at the Federal level, we are going to need your help, and that of your subcommittee and full committee. I am delighted that we began today with the subcommittee chairman, and that you have shown early and strong leadership with regard to the current cancellations.

I appreciate you taking time to come over here. I know you have the Superfund markup. Any questions?

Mr. **GEJDENSON**. May I briefly ask what areas do we presently regulate insurance companies over on the Federal level? What Federal legislation presently regulates them?

Mr. **FLORIO**. Well——

Mr. **GEJDENSON**. In similar kinds of problems as the ones we are looking at today.

Mr. **FLORIO**. Well the McCarran-Ferguson Act effectively precludes the regulation of insurance as a business. But quite frankly, the loopholes that are starting to be developed—in some instances at the request of the insurance industry—are almost getting to be more extensive than the prohibition against Federal regulation.

Last year in the course of the banking deregulation proposal, we had insurance representatives come and ask for Federal laws that would have precluded the ability of some banking interests to utilize State law, I think in South Dakota, to get into the insurance business. It was, of course, somewhat unique to have the insurance industry coming to ask for Federal regulation dealing with the ability to go into the business of insurance.

That has traditionally not been the insurance position. So it is changing very dramatically, and I suspect over the next number of years it will change in even more dramatic ways.

Chairman MILLER. Congressman Coats.

Mr. COATS. Well, I appreciate, Mr. Chairman, your holding this hearing. I think there are an awful lot of questions that are still out there to be answered.

In that regard, I was particularly appreciative of the chairman of the Commerce Subcommittee at the Energy and Commerce Committee indicating that we should look into these questions.

Perhaps with a joint effort between that committee and this committee, we can get the answers to some of these questions. I do know some insurance companies wanted to testify but did not feel that they had adequate notice or time to prepare the necessary information. We should give them that opportunity and we should look into this further.

There are obviously some disturbing questions regarding the whole concept of liability coverage for day care centers. Why are the insurance companies suddenly so concerned? What are the causes of these concerns? What are the risks that we are looking at? Are we exaggerating these risks? Is the media playing up the abuses and sexual abuses that have occurred in some child care centers—overhyped—is that creating a situation that is unrealistic? A lot of questions have to be answered.

A lot of statistics have to be proffered to our committees. I look forward to the opportunity to jointly investigate that and find out the answers to some of these questions. It is a disturbing issue and one that we should look at.

Chairman MILLER. Congressman Rowland.

Mr. ROWLAND. I have no statement at this time.

Chairman MILLER. The first panel that the subcommittee will hear from will be made up of Alyce Chessnoe who is a family day care provider from Burke, VA, and the president of the Northern Virginia Family Day Care Association; Karen Solon who is a family day care provider from Falls Church, VA; Jean Weaver who is the day care coordinator for the YWCA out of Baltimore, MD, and the president of the Maryland Child Care Association; Sandra Gellert, who is the president of the National Association of Family Day Care from Clifton Heights, PA, who will be accompanied by Lori Weinstein who is the director of the Family Day Care Project for the Children's Foundation from Washington, and Deborah Phillips who is the director of the Child Care Information Service for the National Association for the Education of Young Children.

If you will come forward please? We welcome you to the committee. We appreciate your taking your time to come today to share your thoughts and your concerns on this subject. Now we will take you in the order in which I called your names.

Your written statements will be placed in their entirety in the record of this hearing. In order to allow the maximum amount of time for questions from members of the committee to you, we would appreciate your summarization of your statements to the extent that you so desire.

Ms. Chessnoe.

STATEMENT OF MS. ALYCE M. CHESSNOE, FAMILY DAY CARE PROVIDER, BURKE, VA, PRESIDENT, NORTHERN VIRGINIA FAMILY DAY CARE ASSOCIATION

Ms. **Chessnoe.** I have been a family day care provider for over 8 years and it looks like my days in this profession are numbered due to something beyond my control and something I had nothing to do with—namely, the midterm cancellation of my liability insurance and the unavailability of any other similar liability insurance at this time. Most importantly, the working parents and their children would suffer if I do not continue.

The special joys of children are what brought me to be a family day care provider and that, in addition, to the unique relationships we all develop as "extended families" is why I have continued in this profession.

Family day care has allowed me to utilize my training and education, my 10 years experience as both an art teacher and an elementary teacher, my on-the-job training as a mother of 2 boys—now 12 and 13 years old—and my concern for the children that I care for, that all their needs are met.

I have been a family day care provider since January 1977 when I reentered the work force after an absence of 6 years. This was what I chose to do after considering other job possibilities involving working with children and what I would like to do also for many years to come.

The product that we offer is service and through the years, I have been able to provide, in many instances, a unique service to both the children and their families.

How could I ever forget Clay, a pre-teenager who was wrestling with the handicap of his body in a wheelchair while stretching his mind to new heights?

Or, the memories of each new baby that comes and grows and develops . . . memories which in turn, are later shared with these same children, who are delighted as I begin a story with, "I remember you when . . ." Or, how can I ever forget the times that we have been with the families and children in time of crisis and special needs.

By being a stable influence in their little lives, I have tried to ease the tremendous challenge of "getting bigger."

Although the monetary compensation is needed, I am in this profession for the personal satisfaction that comes from being a partner with the family in the wonderful process of nurturing a new baby each year, for example, or of carefully monitoring for five years the special needs of another child with a very unique disease, or of caring for a child through the time span of serving him three meals a day since his parents' work schedule takes them away for such a long time.

My continuance in child care is being threatened by this midterm cancellation of my liability insurance by Mission Insurance Company as of September 1, 1985.

To me, this action leaves many unanswered questions of "why me?" To the parents of whom I serve, they wonder who will care for these special children now?

These unanswered questions continue in my second role, as president of the Northern Virginia Family Day Care Association [NVFDCA] as we ask "why us?"

Our association has a membership of over 170 child care providers located predominantly in Fairfax County. Approximately 90 percent of those members requested, through us, the application and insurance information.

Our outreach is even further, as I visit classes for new providers to tell them about our organization and to encourage them to have liability insurance.

What do I tell them now? In the last 6 months our minimum insurance premium has been raised from $82 to $165 to now being unavailable.

During this same time the liability limit available dropped from $1 million to $300,000. However, all those whose insurance was due for renewals were told that they were not being carried any longer; they were not even given 60 days notice. All others were given midterm cancellation notices effective in approximately 60 days or September 1, 1985.

We have tried to be patient as BMF Marketing Insurance Services, Inc. assured us that they were negotiating with three or four companies to get what we consider both adequate and affordable insurance.

However, we have not to this date been informed of anything definite. In the meantime, our insurance committee has searched out every other possibility that they heard of.

Still nothing. Nothing! No insurance at any rate. No insurance with any special endorsements omitted. No insurance with any exceptions added. Nothing!

Without adequate, affordable insurance, family day care as we know it today will not exist. There are grave concerns among the providers. The general feelings of those that I talked to, who do not have insurance now, is that they would not continue in taking care of children without it.

We, the family day care providers, are giving of ourselves and our families to provide an irreplaceable service of meeting the needs of the children we take care of and their families.

In opening up our hearts and our homes to the child who has special needs, to the newborn and his mother who needs all the support we can muster to help her cope with her anxieties over leaving her baby, to the working parents with long and unusual working hours, to the parent with little income, we hear you.

Where will these working families with their special needs turn to? Who will take care of America's children?

[Prepared statement of Alyce Chessnoe follows:]

PREPARED STATEMENT OF ALYCE CHESSNOE, FAMILY DAY CARE PROVIDER, BURKE, VA

I have been a family day care provider for over 8 years and it looks like my days in this profession are numbered due to something beyond my control and something I had nothing to do with—namely, the mid-term cancellation of my liability insurance and the unavailability of any other similar liability insurance at this time. Most importantly, the working parents and their children would suffer if I do not continue.

The special joys of children are what brought me to be a family day care provider and that, in addition, to the unique relationships we all develop as "extended families" is why I have continued in this profession. Family day care has allowed me to utilize my training in education, my 10 years experience as both an art teacher and elementary teacher, my on-the-job training as a mother of two boys (now 12 and 13 years old), and my concern for the children that I care for, that all their needs are met.

I have been a family day care provider since January, 1977 when I reentered the work force after an absence of 6 years. This was what I choose to do after considering other job possibilities working with children and is what I would like to continue doing for many more years.

The product that we offer is service and through the years, I have been able to provide, in many instances, a unique service to both the children and their families. How could I ever forget Clay a pre-teenager who was wrestling with the handicap of his body in a wheelchair while stretching his mind to new heights? Or, the memories of each new baby that comes and grows and develops . . . memories which, in turn, are later shared with these same children, who are delighted as I begin a story with, "I remember you when . . ." Or, how can I ever forget the times that we have been with the families and children in time of crisis and special need. By being a stable influence in their little lives, I have tried to ease the tremendous challenge of "getting bigger".

Although the monetary compensation is needed, I am in this profession for the personal satisfaction that comes from being a partner with the family in the wonderful process of nurturing a new baby each year, for example, or of carefully monitoring for 5 years the special needs of another child with a very unique disease, or of caring for a child through the time span of serving him three meals a day since his parents' work schedule takes them away for such a long time. My continuance in child care is being threatened by the mid-term cancellation of my liability insurance by Mission Insurance Company as of September 1, 1985. To me, this action leaves many unanswered questions of "why me?" To the parents of whom I serve, they wonder who will care for these special children now?

These unanswered questions continue in my second role, as president of the Northern Virginia Family Day Care Association (NVFDCA) as we ask "why us?"

Our association has a membership of over 170 child care providers located predominately in Fairfax County. Approximately 90 percent of those members requested the application and insurance information. Our outreach is even further, as I visit classes for new providers to tell them about our organization and to encourage them to have liability insurance. What do I tell them now? In the last 6 months our minimum insurance premium has raised from $82 to $165 to now being unavailable. During this same time the liability limit available dropped from $1,000,000 to $300,000. However, all those whose insurance was due for renewals were told they were not being carried any longer; they were not even given 60 days notice. All others were given mid-term cancellation notices effective in approximately 60 days or September 1, 1985.

We have tried to be patient as BMF Marketing Insurance Services, Inc. assured us that they were negotiating with three or four companies to get what we consider both adequate and affordable insurance. However, we have not to this date been informed of anything definite. In the meantime, our insurance committee has searched out every possibility that they heard of. Still nothing. Nothing! No insurance at any rate. No insurance with any special endorsements omitted. No insurance with exceptions added. Nothing!

Without adequate, affordable insurance, family day care as we know it today will not exist. There are grave concerns among the providers. The general feelings of those that I talked to, who do not have insurance now, is that they would not continue in taking care of children without it. We, the family day care providers, are giving of ourselves and our families to provide an irreplaceable service of meeting the needs of the children who we care for and their families. In opening up our hearts and our homes to the child who has special need to the newborn and his mother who needs all the support we can muster to help her cope with her anxieties over leaving her baby, to the working parents with long and unusual working hours, to the parent with little income, we hear you. Where will these working families with their special needs turn? Who will take care of America's children?

STATEMENT OF KAREN E. SOLON, FAMILY DAY CARE PROVIDER, FALLS CHURCH, VA

Ms. SOLON. For hopefully less than 20 seconds, I ask your indulgence while I hand you some photographs that I would like you to look at to give some flesh to the children I refer to in my report. Particularly Erin whose name is mentioned here.

I would like you to keep in mind the child that fits this bathing suit. Her mother is here. She accidentally left it in my home yesterday, we played in the sprinkler. Her mom is here.

My family day care liability insurance was terminated at 12:01 a.m. on July 1, this month. I thank you for the opportunity to address you on behalf of my own children and the children and families I serve in my family day care business. I hope you will find the testimony useful.

My own children are Sarah, age 11 and Simon, age almost 9. We became a single parent family in 1978. Faced with the economic realities, I chose to provide family day care. Fees collected would pay my bills and working at home saved me day care fees I would have had to pay for my young children's care had I worked outside the home.

To me, raising my babies alone, isolated from all relatives, seemed unnatural. I was raised in a small New England village with grandparents, aunts, uncles, and cousins within walking distance. Weekends meant three-generational pot-luck picnics. The adults shared the joys and sorrows and responsibilities of raising a family. We children flitted from relative to relative like hummingbirds in a field of wildflowers, drinking the nectar of their love and spreading love from family member to family member.

The isolation I felt was bad enough. But to leave my children in the care of a stranger seemed unthinkable to me then. Most of my friends were home with their babies, supported financially by husbands.

I worried that I would have trouble relating to women who would leave their children with me. Then the interviews to fill my vacancies began. My kitchen table encounters raised my consciousness. Parents shared with me their deep love for their children and their commitment to their family life. Parents' voices were often tremulous as they contemplated leaving their precious children with a stranger—me. The stories of their agonizing search for the right person are no doubt familiar to this committee. Our needs meshed, and my career in family day care began.

Two and a half years later, I accepted an offer to work part time for the Fairfax County Office for Children as a monitor in the Child Care Food Program. My own children were in school already and my day care children were ready for nursery school as an alternative. Providing after-school care for four of the children provided stability in the relationships we had developed, and supplemented my income. I had a foot in two worlds.

As a monitor, I met well over a hundred family day care providers regularly for 2 years. Those visits convinced me that family day care meets a vital need for many families, and a viable alternative to the traditional extended family. Anecdotes abound of the loving interdependence and support systems provided for the caregivers and the families they serve. I chose to return to family day care as a full time provider, this time with older children, greater energy, and a stronger commitment.

I was slow in renewing my membership in my local day care association and in applying for insurance. A cut requiring three stitches spurred me on. The child lived in a single parent home with a handicapped sibling and no health insurance. I was grateful for my Red Cross training, I blessed the mother for her understanding and applied for liability insurance.

The older children referred to above are my own. The day care children entrusted to me are young. I view infants and very young children as a population at great risk in the child care crunch. Coming back, I knew I just had to have at least one infant, and for many reasons selecting the right parents—parents with philosophies of childrearing compatible with mine—was important.

I met Andrew at 3 months, Shallon at 13 months, and we began. Ryan, about Shallon's age, joined us in September; by January I was ready to add Holli, about Andrews' age.

Ryan's older sister is Erin and she is about to enter second grade. She had just turned 2 years old when I used to tell her nap-time stories about when I was a little girl. How can I express the joy of watching her meet the schoolbus with my son Simon, and how can I tell her she cannot come to my house this fall because I cannot find day care insurance.

Nowhere is it written that we have to become important in one another's lives. But when Shallon's father was hospitalized and her mother was almost delirious with fever—this was at the same time—far from family and in a new neighborhood, my home and my heart were open to support her family in whatever ways I could.

And at the same time, until he succumbed to the flu, Andrew's father transported Shallon to my home. With three of my day care parents out of commission, I transported both children and welcomed the excuse to see in person how Shallon's mother was faring.

Likewise, nowhere is it written that my clients have to nurture my children but they do. How many little "shows" has Erin and Ryan's mother applauded over the years. The tenderness and gratitude they express to my children for the peek-a-boo play and piggyback rides their children enjoy with mine recalls for me the pot luck picnics of my childhood.

Family day care may not be what every family wants nor what every family needs—nor every child needs. But knowing my experiences are not unique to me compels me to be here today. It is not right to force me into the work force outside my home because adequate insurance is unavailable. The school-age child care resources are strained enough without adding my children to the population in need. The resources for infants and toddlers does not need my day care babies. And we want to stay together.

I remarried 3 years ago. I will not jeopardize my husband's assets, saved for his teenage daughters and his aged parents. As a responsible parent and loving wife, I am obligated either to secure adequate liability insurance or to seek alternate employment. Having survived the quicksand of legal fees from my divorce, I cannot knowingly place myself in the position of having someone saying to me, "Talk to my lawyer." for reasons over which I have no control or responsibility, unless I have insurance.

[Prepared statement of Karen Solon follows:]

PREPARED STATEMENT OF KAREN SOLON, FAMILY DAY CARE PROVIDER, FALLS CHURCH, VA

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STATEMENT OF JEAN WEAVER, DAY CARE COORDINATOR, YWCA, BALTIMORE, MD, AND PRESIDENT, MARYLAND CHILD CARE ASSOCIATION

Ms. WEAVER. First of all I would like to thank you for inviting me to come today. I do have testimony that I would appreciate that you have in hand before I read mine.

My name is Jean Weaver and I am the day care coordinator for the YWCA. I am also here to represent another organization which is called the Maryland Child Care Association, which is made up of day care center directors for approximately 80 day care centers in Baltimore City and surrounding counties of Maryland.

I just want to give you some background information about the YWCA. The YWCA of Greater Baltimore has a large day care program—11 sites—with a licensed capacity of over 800 children.

The YWCA also operates three shelters for the homeless and a full range of class and group programs for children and adults.

Several years ago, before the existence of the day care programs or the shelter programs, the Baltimore YWCA had joined with other YWCA's nationwide in obtaining property and liability insurance, with multiyear policies running from July 1 to June 30.

The cancellation problem. Between March 15 and April 15 of this year, the YWCA was notified that our property and liability, our board of directors and officers, and our excess liability insurance were all being canceled.

As we understand it, 45 days' notice of cancellation is obligatory. We were given 45 days' notice on the property and liability, and less than 3 weeks on the Excess Liability.

We had had some property claims, because of a fire at a non-day care site and several small vandalism incidents. There had been no liability settlements, nor were there any actual claims pending.

No reason was given for the cancellation, however, beyond underwriting reasons. We requested the Maryland Insurance Commissioner to look into the matter and received a reinstatement notice to cover us until the 45 days had passed.

We were also informed that the settlement on the fire, which had not originated in the space we rented, exceeded the amount of the premiums we had paid, and that this was part of the reason for our policy being canceled.

The insurance company which had underwritten the YWCA's across the country ceased to work with all YWCA's as a group. We understand that they have accepted YWCA's on an individual basis only if the YWCA does not have day care centers, shelters or team sports programs. Four brokers searched for insurance companies to handle the YWCA's property and liability insurance; we finally obtained property and liability on the 45th day, at 6 p.m. after being turned down by more than 30 companies and having had to make contingency plans to shut down our entire operation.

Obtaining excess liability was equally difficult, and we had to go uncovered by board of directors and officers liability insurance for nearly 2 weeks before a policy was found.

The first property and liability policy which was offered specifically excluded child abuse. We were able, through splitting the policy and setting up the day care policy separately, to obtain this essential coverage.

Although we have not had any claims of this sort, other centers in central Maryland have had claims, and there is always the possibility of such a claim occurring.

Just want to talk a little bit about the increased costs and the decreased coverage. The new policy costs a total of $73,846, compared to the $23,620 for last year.

This is an increase of 212 percent for the entire YWCA for property and liability and excess liability, board of directors' liability, and automobile coverage.

The day care portion increased from $12,150 to $30,000, while deductibles increased and total coverage decreased. A chart is attached to my testimony which gives details.

Our day care centers are a mix of private paying parents, and subsidized parents, for whom the daily rate is fixed by contract. We cannot charge subsidized parents anything beyond the State daily reimbursement rate, which is currently $10 per day, per child, regardless of whether or not our cost per child per day is $10, $12, or $100.

This means that the added insurance costs cannot be passed through to 50 percent of our children, and that either we pass them through to the paying parents or somehow reduce other costs.

Having the private paying parents absorb the total cost of insurance increases would put day care beyond the ability of many parents to pay, and would close entire centers in our system. Our day care program is 4 years old.

We are constantly fighting an operating deficit while fighting to get salaries above minimum wage. Our system has lost money in 3 of its 4 years of operation because of freezes on subsidized placements.

We have been working hard to build the number of full-pay parents. Our current weekly fee runs between $50 and $55. An additional $5 per week per child would simply remove many children from the day care system, force parents to leave their jobs or to leave children unattended.

If we exclude subsidized children from our day care centers so as to pass through the insurance increases more equitably, we will be forcing parents who need to work to leave their jobs, or to leave their children unattended.

There is no help available from other parts of the YWCA, whose budget has been equally adversely affected by insurance increases.

The bottom line for the YWCA is that day care is an economically fragile program at best.

This increase in insurance premiums, or failure to find insurance could push our board to the unwelcome conclusion that we should limit our day care program to the affluent, or, that we should cease to provide the service.

We hate to think of the disruption that such solutions would cause to families who are dependent on us for care. We hate to think that their alternatives would be other providers who are willing to go uninsured, or, even worse, leaving the children unattended.

I have given you an attachment to show you a comparison from last year—what our insurance rates were—as opposed to fiscal year 1986. Total Baltimore YWCA insurance bill for the year ending June 30, 1985 compared to the bill for current fiscal year 1986. Day care property and liability for fiscal year 1985 was $8,600 and for fiscal year 1986 it was $13,468. Other YWCA property and liability last year was $9,244, this year it is $31,428. Excess liability was $2,500, for fiscal year 1986 it is $18 thousand. Board of Directors and Officers was $385 and in fiscal year 1986 it is $1,750. Automobile was $2,891 and fiscal year 1986 it is $8,600. The total package for fiscal year 1985 was $23,680 and the total for fiscal year 1986 is $73,846.

If you notice the coverage comparison—in almost every category, deductibles increased and coverage was lowered. The most striking example is in the excess liability policy which has covered the entire association for $3 million last year for a premium of $250.00 which is not limited to $1 million while the premium is $18,600.

I thank you for allowing me to testify. [Attachment.]

[Prepared statement of Jean Weaver follows:]

PREPARED STATEMENT OF JEAN WEAVER

BACKGROUND

The YWCA of the Greater Baltimore Area has a large day care program (eleven sites) with a licensed capacity of over 800 children. The YWCA operates three shelters for the homeless and a full range of class and group programs for children and adults.

Some years ago, before the existence of the day care programs or the shelter programs, the Baltimore YWCA had joined with other YWCA's nationwide in obtaining property and liability insurance, with multi-year policies running from July 1 to June 30.

CANCELLATION

Between March 15 and April 15 of this year, the YWCA was notified that our Property and Liability, our Board of Directors and Officers, and our Excess Liability Insurance were all being cancelled. As we understand it, 45 days' notice of cancellation is obligatory. We were given 45 days' notice on the Property and Liability, and less than three weeks on the Excess liability.

We had had some property claims, because of a fire at a non-day care site, and several small vandalism incidents. There had been no liability settlements, nor were there any actual claims pending. No reason was given for the cancellation, however, beyond "underwriting reasons". We requested the Maryland Insurance Commissioner to look into the matter, and received a reinstatement notice to cover us until the 45 days had passed. We were also informed that the settlement on the fire, which had not originated in the space we rented, exceeded the amount of premiums we had paid, and that this was part of the reason for our policy being cancelled.

The insurance company which had underwritten the YWCA's across the country ceased to work with all YWCA's as a group. We understand that they have accepted YWCA's on an individual basis only if the YWCA does not have Day Care, Shelter or Team Sports programs. Four brokers searched for insurance companies to handle the YWCA's property and liability insurance; we finally obtained Property and Liability on the 45th day, at 6 pm, after being turned down by more than 30 companies and having had to make contingency plans to shut down our entire operation. Obtaining Excess Liability was equally difficult, and we had to go uncovered by Board of Directors and Officers Liability insurance for nearly two weeks before a policy was found.

The first Property & Liability policy which was offered specifically excluded child abuse. We were able, through splitting the policy and setting up the day care policy separately, to obtain this essential coverage. Although we have not had any claim of this sort, other centers in Central Maryland have had claims, and there is always the possibility of such a claim occurring.

INCREASED COSTS AND DECREASED COVERAGE

The new policies cost a total of $73,846, compared to $23,620 for last year. This is an increase of 212% for the entire YWCA for property and liability, excess liability, Board of Directors' liability and automobile coverage. The Day Care portion increased from $12,150 to $30,000, while deductibles increased and total coverage decreased. A chart is attached to my testimony which gives details.

Our day care centers are a mix of private paying parents, and subsidized parents, for whom the daily rate is fixed by contract. We cannot charge subsidized parents anything beyond the State daily reimbursement rate, which is currently $10 per day, regardless of whether our cost per child per day is $10, $12, or $100. This means that the added insurance costs cannot be passed through to 50% of our children, and that either we pass them through to the paying parents or somehow reduce other costs.

Having the private paying parents absorb the total cost of insurance increases would put day care beyond the ability of many parents to pay, and would close entire centers in our system. Our day care program is four years old. We are constantly fighting an operating deficit while fighting to get salaries above minimum wage. Our system has lost money in three of its four years of operation because of freezes on subsidized placements. We have been working hard to build the number of full-pay parents. Our current weekly fees run between $50 and $55. An additional $5 per week per child would simply remove many children from the day care system, force parents to leave their jobs or to leave children unattended. If we exclude subsidized children from our Day Care Centers so as to pass through the insurance increases more equitably, we will be forcing parents who need to work to leave their jobs, or to leave their children unattended.

There is no help available from other parts of the YWCA, whose budget has been equally adversely affected by insurance increases. The bottom line for the YWCA is that day care is an economically fragile program at best. This increase in insurance premiums, or failure to find insurance could push our Board to the unwelcome conclusion that we should limit our day care program to the affluent, or, that we should cease to provide the service. We hate to think of the disruption that such solutions would cause to families who are dependent on us for care. We hate to think that their alternatives would be other providers who are willing to go uninsured, or, even worse, leaving the children unattended.

Thank you.

TOTAL BALTIMORE YWCA INSURANCE BILL FOR THE YEAR ENDING JUNE 30, 1985, COMPARED TO BILL FOR CURRENT YEAR

	Fiscal year 1985	Fiscal year 1986
Day Care property and liability	$8,600	$13,468
Other YW property and liability	9,244	31,428
Excess liability	2,500	18,000
Board of Directors, Officers	385	1,750
Automobile	2,891	8,600
Total	$23,620	73,846

Coverage comparison: In almost every category, deductibles increased and coverage was lowered. The most striking example was in the Excess Liability policy, which had covered the entire Association for $3,000,000 last year for a premium of $2,500, and which is now limited to $1,000,000 while the premium has increased to $18,600.

STATEMENT OF SANDRA GELLERT, PRESIDENT, NATIONAL ASSOCIATION FOR FAMILY DAY CARE, CLIFTON HEIGHTS, PA

Ms. GELLERT. Mr. Chairman and other distinguished members of the House Select Committee on Children, Youth, and Families, I am delighted to have the opportunity to testify on this very critical issue affecting family day care.

The testimony I am about to give is information gathered by the National Association for Family Day Care from discussions with family day care providers around the country.

The crisis in the liability insurance industry for family day care providers is of critical proportion. During recent weeks, one insurance company after another from Maine to California and Washington to Florida has canceled liability policies for family day care homes.

Only providers in Colorado seem to have temporarily escaped the crisis. The reason being cited for policy cancellation is simply "program dropped."

Two thirds of all the children in day care are in family day care settings. Even more than that, 85 percent of all infants in day care are in family day care settings. There is no questions in our minds that parents of infants could shortly find themselves with no where to turn for their child care needs.

In conversations with providers from various States, several points have come to light. Unless something is done to make adequate affordable liability insurance available family day care providers will go out of business.

The service industry continues to grow. Family day care is a viable small business for single women or as supplemental income in two-parent families.

Without available affordable insurance, women will go elsewhere for work. Existing family day care providers do not want to give up their profession, but will in the face of threatened lawsuits without insurance.

In Arizona and California, providers are homesteading their homes as protection. Infant care will suffer the most. The majority of infants are cared for in family day care settings where the demand is already greater than the supply.

The insurance crisis will decrease the supply even more. Accidents in this age group are numerous and providers will be reluctant to run the risk of caring for infants without adequate coverage.

Many will simply go out of business. I know that quality infant care is of particular importance to this committee. Providers cannot afford high rates currently being charged by some companies.

In a few isolated instances where providers have found liability insurance it is at exhorbitant rates or with restrictions such as limiting care to three or fewer children.

Family day care providers are one of the lowest paid professions. Eighty-seven percent make less than the minimum wage. In many instances, an insurance premium of $759 would be a month's income.

Family day care is unique and more problemmatic and very different from centers or Head Start Programs. Centers may be able to absorb the increased insurance costs; family day care providers cannot.

There have always been fewer underwriters of family day care liability policies to begin with and therefore providers have a harder time obtaining insurance.

The continuation and growth of home-based child care is at a standstill. In several States insurance is mandatory in order to be licensed or registered. In those and many others, new providers cannot get licensed and renewal cannot be processed.

Yet this is at a time when the need for day care is critical. Regulatory experts agree that a lengthy waiting period for certification discourages the people from entering the profession. They go elsewhere. Providers are in the unique position of operating a business out of their homes and are finding other forms of home protection being jeopardized or canceled.

Providers can no longer get business riders for their homeowners policies and in some States have had their homeowner policies canceled because they could not get adequate family day care insurance.

The underwriters of the policy fears for his own liability regarding the other protection. Family day care providers are losing the battle. Family day care providers have had to fight to get and protect what they have.

Each year they rally through meetings and letter writing campaigns to save the Child Care Food Program. This usually after working a 12-hour day.

They join local, State and national associations to improve their professional status and upgrade their own skills at a time when the training funds have been cut and cut.

Family day care providers fight continual battles over adverse zoning and building restrictions. Providers fight to gain recognition and status so other providers will come out from underground, become registered, pay taxes, et cetera. Yet adverse media has blown out of proportion the issue of child abuse in day care when it has been long documented that the vast majority of child abuse happens in the child's own home and day care has been used effectively in treatment of family violence.

At what point do family day care providers just give up in frustration? The pay is low, the stress factor is high. The insurance crisis may just cause them to give up the battle when family day care is really an integral part and necessary to today's economy.

In a society of two parent working families and an increasing number of single parents, the need for family day care has never been greater. As recent as just a few years ago, some parents could afford to stay home until their children were two or three.

Now working mothers must frequently return to their jobs 4 to 6 weeks after having a child. There are no other options. Quality family day care is a necessity to them in the same way that food and housing is. And remember family day care providers are working parents also.

Providers around the country are concerned. Diana Abel of Arizona said, "No new homes are opening there because there is no insurance." Siubhan Stevens in California where a policy is available said, "Providers are quitting because they fear large lawsuits and they cannot affort $750 a year insurance premiums."

Rebekah Short from Pennsylvania said, "The insurance crisis could set the family day care profession back 10 years. All the work to promote quality home care may do down the drain. Some will quit rather than run the risk. Others will operate under the table as they did years ago making it harder for parents to find adequate day care arrangements."

Carol Lynch of Vermont said, "The crisis is affecting employer-sponsored child care programs because the employers want the providers they sponsor to be adequately insured."

The company fears for its own liability. Where insurance is found, the high cost is being passed on to the parents who cannot afford the higher costs. In New Jersey, Sydall Mason of Archway Programs said, "They convinced INA to cover their day care homes because they would cover their centers, but at price of $800 per home." In Delaware County, PA, a title XX program found insurance for its 75 homes but at a price of $1,000 per home.

The National Association for Family Day Care has determined that the availability of infant care in this country is in real jeopardy from this insurance crisis.

There is not enough day care slots now and this will reduce the slots even further. Family day care providers who want to continue in their profession, but not at the risk of losing everything they own in one lawsuit.

Especially when family day care is already one of the lowest paid professions. The risk is greater than the compensation. Now I worry every day because I am a single parent, sole breadwinner for myself and two teenage children.

One lawsuit could destroy my family. Yet, I love what I do and I do not want to be forced into giving up family day care.

My insurance is cancelled, effective September 2, 1985. I fear continuation of my job but I must support my family. My day care families need me, they sympathize, but cannot afford higher rates.

I cannot afford the higher insurance rates and I cannot pass them on to my parents. Today I close by asking each of you on the committee, What are we family day care providers to do? What are the parents of infants who need day care to do when their family day care provider shuts down because she cannot afford the insurance, cannot find insurance, and cannot afford the risk?

Thank you.

[Prepared statement of Sandra Gellert follows:]

PREPARED STATEMENT OF SANDRA GELLERT, PRESIDENT, NATIONAL ASSOCIATION FOR FAMILY DAY CARE

Mr. Chairman and other Distinguished Members of the House Select Committee on Children, Youth and Families:

I am delighted to have the opportunity to testify on this very critical issue affecting family day care.

The testimony I am about to give is information gathered by NAFDC from discussions with family day care providers around the country.

The crisis in the liability insurance industry for family day care providers is of critical proportion. During recent weeks, one insurance company after another, from Maine to California and Washington to Florida, has cancelled liability policies for family day care homes. Only providers in Colorado seem to have temporarily escaped this crisis. The reason being cited for policy cancellations is simply, "Program dropped."

Two thirds of all children in day care are in family day care settings. Even more than that, 85% of all infants in day care are in family day care settings. There is no question in our minds that parents of infants could shortly find themselves with nowhere to turn for their child care needs.

In conversations with providers from various states, several points have come to light. Unless something is done to make adequate affordable liability insurance available:

Many family day care providers will go out of business. The service industry continues to grow. Family day care can be a viable small business for single women or it can provide an important supplemental income to two-parent families. Without available affordable insurance, women will go elsewhere for work. Existing family day care providers don't want to give up their profession, but will in the face of threatened lawsuits without insurance. In Arizona and California, providers are homesteading their homes as protection.

Infant care will suffer the most. The majority of infants are cared for in home day care settings where the demand is already greater than the supply. The insurance crisis will decrease the supply even more. Accidents in this young age group are numerous, and providers will be reluctant to run the risk of caring for infants without adequate coverage. Many will simply go out of business. I know that quality infant care is of particular importance to this committee.

Providers cannot afford high rates currently being charged by some companies. In a few isolated instances where providers have found some liability insurance, it is at exorbitant rates or with severe restrictions such as limiting care for 3 or fewer children. Family day care providers are one of the lowest paid professions. 87% make less than minimum wage. In many instances, an insurance premium of $750 would be at least a month's income.

Family day care is unique and more problematic and very different from centers or Head Start Programs. Centers may be able to absorb increased insurance costs; family day care providers cannot. There have always been fewer underwriters of family day care liability policies to begin with, and therefore providers have a harder time obtaining insurance.

The continuation and growth of home based child care is at a standstill. In several states insurance is mandatory in order to be licensed or registered. In those states and many others, new providers cannot get licensed and renewals cannot be processed. Yet this is at a time when the need for day care is critical. Regulatory experts agree that a lengthy waiting period for certification discourages the people from entering the profession. They simply go elsewhere.

Providers are in the unique position of operating a business out of their homes and are finding other forms of home protection being jeopardized or cancelled. Providers can no longer get business riders for their homeowners policies and in some states have had their homeowner policies cancelled because they could not get adequate family day care insurance. The underwriting of the policy fears for its own liability, regardless of other protections.

Family day care providers are losing the battle. Family day care providers have had to fight to get and protect what they have. Each year they rally through meetings and letter-writing campaigns to save the Child Care Food Program. This is usually after working 12 hour days. They join local, state and national associations to improve their professional status and upgrade their own skills at a time when training funds have been cut and cut. Family day care providers fight continual battles over adverse zoning and building restrictions. Providers fight to gain recognition and status so other providers will come out from underground, become registered, pay taxes, etc. Yet adverse media has blown out of proportion the issue of child abuse in day care, when it has long been documented that the vast majority of child abuse happens in a child's own home! Day care has been used very effectively in the treatment of family violence.

At what point do family day care providers just give up in frustration? The pay is low; the stress factor is high. The insurance crisis may just cause them to give up the battle when family day care is really an integral part and necessary to today's economy.

In a society of 2-parent working families and increasing numbers of single parents, the need for family day care has never been greater. As recent as just a few years ago, some parents could afford to stay home until their children were 2 or 3. Now working mothers must frequently return to their job 4-6 weeks after having a child. There are no other options! Quality family day care is a necessity to them the same way food and housing is. And remember, family day care providers are working parents, also.

PROVIDERS AROUND THE COUNTRY ARE CONCERNED

Diana Abel of Arizona said, "No new homes are opening because there is no insurance." Siubhan Stevens in California, where a policy is available, said, "Providers are quitting because they fear large lawsuits and can't afford the $750 a year insurance premium." Rebekah Short from Pennsylvania said, "The insurance crisis could set the family day care profession back 10 years. All the work to promote quality home care may go down the drain. Some will quit rather than run the risk. Others will operate under the table as they did years ago making it harder for parents to find adequate day care arrangements." Carol Lynch of Vermont said, "The crisis is affecting employer sponsored child care programs because the employers want the providers they sponsor to be adequately insured." The company fears for its own liability. Where insurance is found, the high cost is being passed on to the parents who cannot afford the higher costs. In New Jersey, Sydall Mason of Archway Programs said, "They convinced INA to cover their day care homes because they cover their centers, but at a price of $800 per home." In Delaware Co., Pennsylvania, a Title XX program found insurance for its 75 homes, but at a price of $1,000 per home.

The National Association for Family Day Care has determined that the availability of infant care in this country is in real jeopardy from this insurance crisis. There are not enough day care slots now and this will reduce the slots even further.

Family day care providers who want to continue in their profession, but not at the risk of losing everything they own in one lawsuit, especially when family day care is already one of the lowest paid professions. The risk is greater than the compensation. Even an unfounded lawsuit could wipe out a family day care family with court costs and lawyer fees.

As a provider for 12 years myself, I know I never worried about lawsuits until a couple of years ago when day care started getting so much media attention. Now I worry every day because I am a single parent, sole breadwinner for myself and two teenage children. One lawsuit could destroy my family. Yet, I love what I do and don't want to be forced into giving up my family day care profession. My insurance is cancelled effective September 2, 1985. I fear continuation of my job but I must support my family. My day care parents need me, they sympathize, but cannot afford higher rates. I cannot afford the high insurance rates and I cannot pass them on to my day care parents.

Today I close by asking each of you on the committee, "What are we family day care providers to do? What are the parents of infants who need day care to do when their family day care provider shuts down because she cannot afford the insurance or cannot find insurance and cannot afford the risk?"

STATEMENT OF DEBORAH PHILLIPS, PH.D., DIRECTOR, CHILD CARE INFORMATION SERVICE, NATIONAL ASSOCIATION FOR THE EDUCATION OF YOUNG CHILDREN, WASHINGTON, DC

Ms. PHILLIPS. Mr. Chairman, I want to thank the select committee for inviting the National Association for the Education of Young Children to participate in this extremely important hearing on the insurance crisis in child care.

My name is Deborah Phillips. I am speaking on behalf of the National Association for the Education of Young Children [NAEYC] as director of their Child Care Information Service.

NAEYC is a nonprofit, membership association comprised of 47,000 individuals, the vast majority of whom work directly in child care programs and nursery schools.

The loss and unaffordability of insurance is a real crisis in the child care field. It is a crisis that is jeopardizing the availability, the stability, and the quality of child care in this country at a time when this committee has documented an unprecedented need for more and higher quality child care.

It is a crisis because it is affecting child care programs in every State, programs of every type—day care centers, family day care homes, preschools, Head Starts—and programs that serve families from all income brackets, regardless of their quality, regardless of how long they have been in operation and regardless of whether they have ever had an insurance claim.

NAEYC is receiving 200 calls a week from child care providers who cannot find affordable insurance, if they can find insurance at all.

We have never received this magnitude of calls on any issue in the 60 year history of the association. The only available national survey of child care providers conducted by the Child Care Action Campaign and the Child Care Information Exchange at the beginning of the summer, suggests that over two-thirds of the child care programs surveyed are facing serious problems with insurance.

There is likely to be a new wave of nonrenewals, cancellations, and rate increases by late August or early September, which is when most child care programs renew their insurance policies.

I want to give you a feel for what we are hearing from the field by highlighting several themes that are reiterated again and again by the numerous child care providers who are calling us.

First, the loss of insurance and the prohibitive rate increases we are seeing bear no relation to the professionalism, quality or claims history of the programs affected.

Even our Nation's very best child care programs are having problems obtaining affordable liability coverage. The example of NAEYC's liability policy is instructive because the child care centers affected are among the very best this country has to offer and their directors represent the most professionally oriented individuals in the field.

The liability policy offered by NAEYC has had one underwriter withdraw completely, despite their having suffered no losses in conjunction with the NAEYC policy.

After a year and a half delay, we have been able to renegotiate a policy for our members with a new carrier. It has an exclusion for child abuse claims and stringent quality standards are applied as a precondition for programs to receive the insurance. Family day care providers are not included.

Second, insurance is an absolute necessity for the child care field. Providers must have insurance, not only as an essential protection, but also because programs without insurance are operating illegally in half of the States and are therefore ineligible to receive essential Federal funds.

Twenty-four States require all child care centers to have liability insurance and about 7 States include these requirements for family day care, a requirement most recently enacted in California. Without insurance, programs in these States are operating illegally and are technically ineligible to receive Federal funds through title XX or the Child Care Food Program.

If funds end up being withdrawn, many publicly-supported programs will either fold or deteriorate in quality.

Third, many child care programs are unwilling or unable to pass the increased insurance costs onto the families they serve. The greatest pressures along these lines are felt by programs that serve publicly-subsidized families and other low-income families.

Head Start programs and programs that serve title XX children are simply unable to pass increased insurance costs on to their families, because they receive a set reimbursement rate per child. There are no parent fees to raise.

For other programs that serve primarily poor and low-income families, their ability to recoup the insurance costs from parents is limited by the families' ability to pay.

Fourth, programs are sacrificing the quality of the care they provide and are foregoing program improvements to cover their increased costs.

There is no maneuvering room in a child care budget. These programs operate on a shoestring. About 70–80 percent of the average child program's costs go toward staff salaries.

Rent, food, and insurance are set costs, leaving only nonessential materials and staff-related expenses open to cutbacks.

We are hearing that programs are considering increases in the numer of children supervised per adult, hiring staff with less training, reductions in in-service training and cut-backs in the educational resources they make available to children. These are precisely the aspects of program quality that were revealed by this committee last year to bear a direct association to the safety, health, and development of children in child care.

Fifth, the insurance industry is establishing conditions and standards for insurability that are far in excess of any standard that child care providers must presently meet.

By establishing stringent standards of quality that exceed current practice by most child care programs, the insurance industry is effectively writing off child care.

In our own insurance plan, programs are individually assessed using a set of standards that NAEYC established to promote quality improvement in the child care field.

They are high quality, model child care standards. They were never intended to serve as a benchmark against which to judge all child care programs.

Our liability policy first became available last month so we do not know how many programs that apply for coverage will be denied as a result of these stringent conditions. Nor do we know how the rates will compare to our previous rates.

There is a real and a sad irony in this situation because the child care providers who are calling us now are the same providers who have worked with NAEYC and other organizations to establish standards, incentives and funds to support a higher quality of child care in this country.

Now they are paying the price of the lack of Federal standards and the extremely minimal standards that exist in many States.

The link between standards and insurability also catches child care providers in an impossible double-bind. Do they forego program improvements to pay for insurance? Or, do they pay for the improvements and hope that their insurance rates are not tripled? Very few programs can afford both.

I am very worried about the future of child care in the wake of this crisis. Child care has historically been viewed by our society as a necessary evil.

The field has withstood the severe cutting of Federal funds at the beginning of this decade, the recent assault arising from headlines about child abuse, and the ongoing lack of rewards or respect for child care providers. All of these problems have failed to impede the field's commitment to assuring that families who need child care receive it.

But this insurance crisis is different. No matter how hard or how long a provider has worked to create a high quality program, in just 60 days they can find themselves facing the responsibility of caring for children without insurance.

The real victims, however, are the children. Whatever extra resources can be found in the child care market will not go to insurance companies rather than to higher staff-child ratios, better trained staff, or retention of staff and these are the true means of insuring the healthy care of children in child care.

Thank you very much.

[Prepared statement of Deborah Phillips, Ph.D., follows:]

PREPARED STATEMENT OF DEBORAH PHILLIPS, PH.D., DIRECTOR, CHILD CARE INFORMATION SERVICE, NATIONAL ASSOCIATION FOR THE EDUCATION OF YOUNG CHILDREN, WASHINGTON, DC

Mr. Chairman, I want to thank the Select Committee for inviting the National Association for the Education of Young Children to participate in this extremely important hearing on the insurance crisis in child care.

My name is Deborah Phillips. I am speaking on behalf of the National Association for the Education of Young Children (NAEYC) as director of their Child Care Information Service. NAEYC is a nonprofit, membership association comprised of 47,000 individuals who work in all facets of early education. The vast majority of our members work directly with children in child care programs and nursery schools. They all approach their work with a strong sense of professionalism; with a commitment to self-improvement; and a determination to work with us toward the goal of improving the quality of child care and early education programs in this country.

This is a real crisis.

It is a crisis that is jeopardizing the availability, stability, and quality of child care in this country at a time when this Committee has documented an unprecedented need for more and higher quality child care. Child care is integral to the self-sufficiency of millions of today's families. Under these circumstances, the sweeping and dubious classification of child care as being of extremely high risk and its associated vulnerability to boom-bust patterns of insurability are intolerable.

It is a crisis because it is affecting child care programs in every state, programs of every type—centers, family day care homes, preschools, profit and nonprofit, church-sponsored and community-sponsored, and Head Start—and programs that serve families from all income brackets; Regardless of their quality, Regardless of how long they have been in operation, and Regardless of whether they have ever had an insurance claim.

MAGNITUDE OF THE PROBLEM

NAEYC is receiving 200 calls a week from child care providers who cannot find affordable insurance, if they can find insurance at all. We have never received this magnitude of calls on any issue in the 60 year history of the Association.

The only available national survey of child care providers, conducted by the Child Care Action Campaign and the Child Care Information Exchange at the beginning of the summer, suggests that over two-thirds of the child care programs surveyed are facing serious insurance problems, and that there is likely to be a new wave of non-renewals, cancellations, and rate increases by late August or early September when most child care programs purchase their insurance.

Twenty percent of the programs that returned survey forms had had insurance cancelled or not renewed.

Another 30 plus percent had had their rates increased by over 100%.

Increases of 300% were not at all uncommon—a finding that is corroborated by the calls we have received at NAEYC.

And, approximately 20% of the programs reported "no problem", but were insured by companies which have since begun to cancel policies or substantially increase rates.

In Michigan, a survey conducted by the State Department of Social Services in June of this year revealed that, of 86 child care centers responding, half had had their liability policies cancelled or not renewed. Of the programs whose insurance policies had been retained, two experienced significant rate increases, one rising from about $500 per year to $2250.

The program manager for Day Care Services who oversaw the study noted that there appears to be no relation between cancellations, nonrenewals, and a program's history of insurance claims.

In Indiana, a survey conducted by the Indiana Day Care Association tells the same story. Sixty-five child care centers returned survey forms, including two programs that sponsor 250 children served in family day care homes. About 7,000 children are served by these 65 programs.

One-quarter of the programs had had their liability insurance cancelled or were pending cancellation. One-third of the programs had had their rates increased anywhere from 10% to 400%, with the average increase amounting to 125%. Seven of the programs responding had had insurance claims that amounted to less than $100. Two programs had insurance claims of $1,000 and $1,500, respectively.

There was no relation between the programs experiencing cancellations and rate increases and those that had had claims. In fact, the woman who conducted the study noted that programs that had filed insurance claims appeared to have experienced fewer cancellations and smaller rate increases.

I am not here today to judge whether the insurance crisis is fueled by speculation or solid evidence. I have spent hours talking to representatives of the insurance industry, to individual insurers, and to underwriters. They are feeling financial pressures that are forcing them to scrutinize their own policies. They are caught with us in the midst of a highly litigious society. And, child care is not the only industry affected. This is a problem shared by foster homes, obstetricians and gynecologists, nurse midwives, and the cities.

The fact remains, however, that child care is in a highly precarious and volatile position.

I want to give you a feel for what we are hearing from the field by highlighting several themes that are reiterated again and again by the numerous child care providers who are calling us.

First, the loss of insurance and the prohibitive rate increases we are seeing bear no relation to the professionalism, quality, or claims history of the programs affected. Even our nation's very best child care programs are having problems obtaining affordable liability coverage.

One program in Indiana directed by a registered nurse, with highly trained staff and excellent staff-child ratios, had its overall annual insurance premium raised from $3,200 to $9,900, after calling 15 insurance companies that would not even consider writing a policy for her. This program has never filed an insurance claim.

A center in California directed by a teacher with a master's degree in early education, that has operated for 29 years without an insurance claim has had its overall rates raised from $8,000 to $25,000 per year.

The example of NAEYC's liability policy is instructive because the child care centers affected are among the very best this country has to offer and their directors represent the most professionally-oriented individuals in the field.

The liability policy offered by NAEYC has had one underwriter withdraw completely, despite their having suffered no losses in conjunction with the NAEYC policy. We were able to find a new underwriter, although the second policy also reached a very precarious point even before it was offered. It was saved only by negotiating an exclusion for child abuse claims and stringent quality standards as a precondition for acceptance of a program into the plan.

Second, insurance is an absolute necessity for the child care field. Providers must have insurance, not only as an essential protection, but also because programs without insurance are operating illegally in over half of the states and are therefore ineligible to receive essential federal funds.

Over half of the states require that child care centers have liability insurance and about 11 states include this requirement for family day care—a requirement most recently enacted in California.

Without insurance, programs in these states are operating illegally and are technically ineligible to receive federal funds through Title XX, or the Child Care Food Program. Even the Dependent Care Tax Credit requires that parents using child care programs that enroll more than 6 children use licensed programs. If funds are actually withdrawn, many publicly-supported programs will either fold or deteriorate in quality.

Third, many child care programs are unwilling or unable to pass the increased insurance costs onto the families they serve. The greatest pressures along these lines are felt by programs that serve publicly-subsidized and other low-income families.

Head Start programs and programs that serve Title XX children are simply unable to pass increased insurance costs on to their families, because they receive a set reimbursement rate per child. There are no parent fees to raise.

For other programs that serve primarily poor and low-income families, their ability to recoup the insurance costs from parents is limited by the families' ability to pay.

Three actual case examples will offer a handle on the amounts we are dealing with here.

A family day care home in California that has operated for five years without any insurance claims had its rates increased from $100 a year to $800 a year. She cares for 3 children from two families. If she passed the costs on to her parents, they would be charged an additional $350 per year. This is more than one month's payment for full-time child care in her program. She had never had a claim filed against her insurance in the 3½ years she had been in operation.

The child care center in Indiana, directed by a registered nurse, that I mentioned earlier would need to charge its families an additional $144 per year to cover the $6,000 increase in insurance premiums.

The California center that is facing the jump from $8,000 to $25,000 would need to charge each family an additional $100 to cover this increase. About 40% of the families served by this program are low-income and about a quarter are single parents.

Fourth, programs are sacrificing the quality of the care they provide and are foregoing program improvements to cover their increased insurance costs.

There is simply no maneuvering room in a child care budget—the majority of programs are nonprofit, and they operate on a shoestring. About 70-80% of the average child care program's budget goes toward staff salaries. The remainder covers resource materials, physical repairs, rent or mortgage payments, food and insurance. Rent, food, and insurance are set costs, leaving only nonessential materials and staff-related expenses open to cutbacks.

Programs are considering increases in the number of children supervised per adult, hiring staff with less training, reductions in in-service training, and cutbacks in the educational resources they make available to children. These are precisely the aspects of program quality that were revealed by this Committee last year to bear a direct association to child safety and to the healthy development of children in child care.

Yesterday, I talked to a provider in Woodland Hills, California who told me she was preparing to tell her staff that they should not expect any salary increase this year, that she would not hire the extra aides she routinely hires, and that they would not be purchasing any new materials for the children. Her insurance bill, like one of the programs described earlier, jumped from $8,000 to $25,000 for a program enrolling 150 children.

Over the last several weeks, our NAEYC staff have been training providers in Texas, Florida, and Northern and Southern California to assess child care quality in conjunction with our newly-launched Center Accreditation Project. This project is an entirely voluntary effort, originating from within the child care field, to promote the expansion of high quality child care in this country.

The field has been extremely excited about this opportunity to "prove its worth", but our trainers are now hearing from child care directors in each of the three states that they cannot afford to participate in the Accreditation Project because they need the money for insurance, yet they are afraid that without the stamp of approval provided by the Accreditation they won't be able to find insurance.

Even providers who have not yet experienced insurance rate increases or cancellations are postponing improvements and pinching corners so they have funds in reserve when their time comes to pay higher premiums.

Fifth, the insurance industry is establishing conditions and standards for insurability that are far in excess of any standard that child care providers must presently meet.

By establishing standards of quality that far exceeds anything that has been required before, and thus far exceeds current practice by most child care programs, the insurance industry is effectively writing off child care programs.

In our own insurance plan, programs are individually assessed using a set of standards we established to promote qualitative improvements in the child care field. They are high quality, model standards that were never intended to serve as a benchmark against which to judge all child care centers, but rather as a set of goals for programs to achieve following a lengthy self-evaluation. Since this liability policy first became available last month, we do not know how many programs that apply for coverage will be denied as a result of these stringent conditions. Nor do we know how the rates will compare to our previous rates.

I learned from one of the few remaining insurance companies that is still writing policies for family day care providers that they are requiring ratios of 1:3 for infants and 1:6 for preschoolers, and raising rates if the home has a pet or a swimming pool, if the children are taken on field trips, or if they offer gymnastics or dance lessons.

There is a real sad irony in this situation, because the child care providers who are calling us now about insurance are the same providers who have worked with NAEYC and other organizations to establish standards, incentives, and funds to support a higher quality of child care in this country. Now they are paying the price of the lack of federal standards and the extremely minimal standards that exist in many states.

The link between standards and insurability also catches child care providers in an impossible double-bind. Do they forego program improvements—the extra staff person, the in-service training—to pay for insurance or do they pay for the improvements and hope that their insurance rates are not tripled? Very few programs can afford both.

A provider in California explained to me that parent fees would need to be raised 5% to cover her tripled insurance costs, but a 40% fee increase would be required to cover the costs of the program improvements recommended by her insurance company to assure that her coverage will be continued in the future.

CONCLUSION

I am very worried about the future of child care in the wake of this crisis. Child care has historically been viewed by our society as a necessary evil. The field has withstood the severe cutting of federal funds at the beginning of this decade, the recent assault arising from headlines about child abuse, and the on-going lack of rewards or respect for child care providers. All of these problems have failed to impede the field's commitment to assuring that families who need child care receive it.

But this insurance crisis is different: No matter how hard or how long a provider has worked to create a high quality program, in just 60 days they can find themselves facing the responsibility of caring for children without insurance. It is the unpredictability and the complete disregard for an individual provider's efforts to run a good child care program that makes this different from previous crises.

And, we are seeing signs that committed providers and directors of quality programs are simply giving up. Ironically, it is some of our most conscientious providers who are feeling the pressures most acutely, because they are unwilling or unable to pass the increased insurance costs onto the families they serve, and they are unwilling to run a program whose quality of care has been seriously eroded or to operate without insurance.

The real victims, however, are the children Whatever extra resources can be found in the child care market will now go to insurance companies rather than to higher staff-child ratios, better trained staff, or retention of staff who are being drawn away from child care by more lucrative jobs—the true means of insuring the safe and healthy development of children in child care.

I cannot adequately stress the importance of working with the insurance industry, and with your colleagues in Congress to ensure that the immediate insurance crisis is alleviated and that its inevitable return in a few years is prevented. The National Association for the Education of Young Children will, of course, offer any assistance, information, and support as you develop an effective method for addressing this crisis.

Mr. Coats. Thank you. Well you all paint a pretty dismal picture, here, of the insurability or, at least, the willingness of insurance companies to provide insurance. It is a disturbing trend. The question that comes to my mind, and I am sure everybody's mind, is: Why suddenly are insurance companies either completely pulling out of the field, or raising their premiums and standards so high that it makes it almost impossible for day care centers to comply with the cost or the terms?

I am wondering—and I just open this question to anybody on the panel—I am just wondering—surely when you received your notice you called the insurance company or called your agent to ask the same question: What has happened? Why? What is the explanation?

I am interested in what you heard back from the insurance people as you did your investigations, as you searched out new insurance—primarily, when you made that initial call—when I get a $5 increase in my auto premium, I call up my agent and say, "I have not had an accident, I have not had a ticket. What are you talking about? Why are my rates going up."

I can imagine what your reaction was when you received a 200 percent, 300 percent increase, or worse, a cancellation notice. You had to call and say, "Why? What is the answer?"

Ms. **Solon**. First of all, I have not yet gotten around to writing to the one that canceled me because I know Alyce is right on top of that in talking to the people and I am in touch with Alyce. I am going to wait a little bit and see. There was a little bit of a frightening notice that I had to ask within 90 days in writing or I may not even get an answer so I will do that.

Second, I did call yesterday and—before I had an opportunity to write the report—my homeowners insurance company, which is USEA, one of the things that was repeated to me reminded me of why I had not really paid much attention to homeowners in the first place. They only insure me for up to three children. That leaves out Erin who is in the picture, who has been with me since she was two.

The reason for that, they made very very clear to me in a kind of appeal, that their State insurance manuals prohibit them from insuring professional services and commercial operations. They are allowed to insure my operation only if it is incidental to owning my home.

As soon as I start talking professional then there is another, for me very frightening implication, I may be fortunate in having only homeowners because I am not a professional to an insurance agent.

Therefore, I do not have the exemption for failure to provide professional service. So I can sit back and say, "Gee, that is terriffic." However, that is up to a judge to decide, what is professional and what is not professional. I have no way to know what I am insured for and what I am not, being a family day care provider. A certified teacher at least gets an answer to that. I will let someone else go on from here.

Ms. **Gellert**. I have talked with several insurance agents and several insurance companies, all of whom have cancelled providers in various States across the country and the answer I always get seems to come back to one thing.

Either they claim they have realized very large claims or their fear is that they are going to have real large claims and they are going to cancel everybody before they have them.

Mr. **Coats**. Why do they have these fears? What are the claims arising from?

Ms. **Gellert**. No one seems to want to share that information. That seems to be a factor that when you come down to asking the question of: Well where are these documented claims? Nobody wants to part with the information to tell you where they are documented.

Mr. **Coats**. Well, do you think there is a conspiracy underway among insurance companies? Are they getting together and saying, "Look, we do not like day care so we are going to cancel out all the policies?"

Chairman **Miller**. Do you want to ask this audience that?

Ms. **Gellert**. My personal opinion, I would say yes to your question.

Ms. **Weaver**. If I can inject also—what we were told is that day care centers are high-risk businesses. Therefore, they are not insuring any high-risk business.

The first time we approached the companies about why we were being canceled, they told us that it was underwriter's reasons and they did not have to give us an answer.

Of course, our next stop was with the Maryland Insurance Commissioner to say: "Why are we being canceled?" and he informed us that the insurance companies do not have to give us a reason as to why we are being canceled. The thing he kept emphasizing was: "Because of all the media hype about child abuse going on in day care centers," we are classified as high risk.

Mr. **Coats**. Well, that's what I'm trying to get to. That is, is it based on experience? Are they giving you answers like: "Look, this is our experience: we are losing $2 for every dollar of premium?" Generally, that is the way insurance rates are based—actuarial experience. Or is it, "We are concerned about what might happen given all these stories from the media and so forth, about sexual and child abuse, poor standards, health problems, and so forth. It is just a risk that we find unacceptable." Are they getting in to that much detail and depth with you?

Ms. **Weaver**. OK, based on the national statistics, they will not release that information. Insurance companies will not release that information in terms of how many claims they have had against them.

It has been like pulling tooth and nails, trying to get that information from them. Perhaps maybe you can help.

Mr. **Coats**. We have a couple of statistics here, and I just want your reaction to them. For instance, St. Paul Fire and Marine Insurance Co. gave us some statistics. They said in 1982 they took in $667,000 in premiums and paid out $289,000. So they did all right there.

In 1983, they took in $649,000 in premiums but paid out $3,000,000 in claims. In 1984 they took in $308,000 and paid out nearly $5 million in claims. So based on that, St. Paul is saying: "Look, we have not increased our premium total amount coming in; but, our claim experience is just going out of sight and that is why we have to cancel ——."

Mr. **Gejdenson**. Will the gentleman yield?

Mr. **Coats**. Yes.

Mr. **Gejdenson**. Did they indicate what those claims were the result of normal accidents that increased, or are we talking sexual abuse problems?

Mr. **Coats**. I do not have the answer to that. I think that is one thing this committee should try to find out.

Mr. **Gejdenson**. Hopefully the insurance industry will come in because I think it certainly is frightening. In our State, the Head Start Program suddenly found itself without insurance. There are a number of other providers that are terribly nervous about their situation. One of the things we need to address is what is happening. It seems that those are certainly astounding changes and it would be interesting to find out whether it is as a result of litigation or other actions that led to those losses.

Mr. **Coats**. I agree with the gentleman. I am wondering—let me ask you in your own practical experience—have your claims gone up? Have your insurance companies come back to you and said, "Look, your association, your group, has paid this much in premiums but these are the claims we have paid," or, "This is the kind of litigation we are facing." When I call my insurance agent about my car insurance or house insurance, he always says, "Hey there are just so many accidents here in northern Virginia. We have to keep raising these premiums. We have double the amount of cars, the claims are going up, the lawsuits are going up. I am sorry. I know you have not had any accidents, but insurance spreads the risk and you are going to have to pay for all the excess stuff that has been happening." Are they telling you that kind of thing? Are they getting back to you? Are you getting any answers back?

Ms. **Weaver**. OK. We have not had one claim against us in the 4 years we have been operating child care centers. You can see that with not one claim against us, what has happened in 1985 as opposed to 1986.

Mr. **Coats**. Now that is the YW in the Baltimore area?

Ms. **Weaver**. That is right.

Mr. **Coats**. You have not had one claim?

Ms. **Weaver**. Not one claim.

Mr. **Coats**. What about YW nationwide, do you have any idea?

Ms. **Weaver**. I am not sure what has happened nationwide but certainly as to Greater Baltimore in Baltimore, MD, the YW in Baltimore City, we have not had any problems.

We have child care centers throughout the entire State of Maryland.

Mr. **Coats**. Do you think they are trying to tell you that they are worried about what might happen rather than what has happened?

Ms. **Weaver**. We are assuming just that.

Ms. **Gellert**. I have been involved with the Pennsylvania Family Day Care Providers Association since its inception and we did sponsor the liability insurance program for Pennsylvania providers and to my knowledge we have never been given any kind of feedback as to how many providers in Pennsylvania filed claims, to have any idea what percentage of claims against the premiums are being processed but personally, in terms of providers that I come in contact with on a daily basis, which probably number somewhere around 100 to 200 off and on, I do not know of any of them who have ever filed a claim against their liability insurance policy. Yet the rates keep going up, up, up.

Mr. **Coats**. But somebody has to be filing claims. The amount of claims paid in just one company is dramatically increased.

Ms. **Phillips**. I think it is very important to ask that company if those claims are coming from child care programs. They lump a lot of different kinds of their insurance together when they report those numbers. It is very difficult to get to the bottom of some of those numbers. We have tried to do it and we face the same problems with lack of information.

NAEYC's policy was canceled. The company had experienced no losses whatsoever at the time they canceled it. Second, there was a survey conducted in your own State of Indiana by the Indiana Day Care Association. The conclusion from that study, which found that one-quarter of the programs, center-based and family day care, had had their liability insurance canceled, a third had had their rates increased anywhere between 10 and 400 percent, the conclusion was that there was no relationship whatsoever between programs that had experienced claims and those that had not.

And in fact, there seemed to be an inverse relationship so that programs that had had claims, and they are talking very small—$200 minor accident minor accident claims in this case—were able to retain their insurance and those that had not had any claims were having their policies canceled.

That is one of the worst things that is going here. It is—there is no relationship. You cannot predict what is going to happen to your own program, based on your own quality, and your own claims' history.

Chairman **Miller**. Does the gentleman yield?

Mr. **Coats**. Yes.

Chairman **Miller**. I think it is becoming clearer that the insurance industry should come to the committee and explain exactly what is going on. In our discussions over the past month with the insurance industry, it appears that the panic within the industry that has caused these cancellations or 60-day notices has been generated by media reports of child abuse and sexual molestation. Yet, we have yet to have a company suggest to us that there has been a single such claim.

In fact, many of these policies exclude claims for abuse. St. Paul has told us that they do not have any such claims. They have what appears to be a pending claim somewhere in the Western United States that may have some anticipated losses.

Now, I do not know whether your $3 million figure or mine is accurate. It is clear that the industry is saying different things to different folks. Worse they are not saying anything to their clients to try to assure them of the reasons for the cancellation.

We were told the same thing when we began: "Well, this is an industry determination. This is a company decision." That is not terribly helpful to people who must then turn and explain it to the parents who need child care for their children.

I know that the minority staff has been as frustrated as the majority staff has been in trying to get an answer to the core question: Why this treatment by the industry? We get, "We do not know." It is a little hard to design a proper response, whether at the State or Federal level, or within the industry. It has been frustrating.

At this point, I'd have to say we have not had any substantiation of economic losses related to the child care claims.

The issue of whether premiums have been too low and have not been increased over a period of years is open to question. But the risk of losses from child care claims leading to wholesale cancellations within this industry, so far has not been substantiated. I am told by Mr. Gejdenson that the industry will soon be prepared to testify. I hope with Mrs. Johnson's help and Mr. Gejdenson's help, we can get that gigantic industry from Connecticut to come in and to shed some light on this. I am sorry for taking the gentleman's time. I will extend him additional time.

Ms. CHESSNOE. Mr. Chairman, may I address—first of all, to Mr. Coats. One reason why we have not called up the particular insurance company at this point is that when one gets such a nonpersonal piece of paper as this that is run out of a computer, one after another, the reason being simply, "program being discontinued," we feel like this is closing the door—"do not call us and we are not going to call you."

Mr. COATS. You know they insure millions and millions of people; and, they, like all the rest of us, have to operate on a computerized basis. I wish life were not like that. I get those notices at home, but we all have agents that we deal with——

Ms. CHESSNOE. Yes but we have also tried to call——

Mr. COATS. Do you have an agent that you deal with?

Ms. CHESSNOE. Right and the particular one has tried to be encouraging to us that they, in essence, are dealing with three or four other companies. However, unless we pay a premium and unless we have a policy in our hands, we are not insured.

And all the hope and expectations are not good enough. They can say, "we are trying," but we have to say, "unless we actually have the policy in our hands, we are not insured." And right now we are not insured.

Mr. COATS. I understand that, but I do not understand why you would not pursue it on a person-to-person basis.

[Voice from the audience, inaudible.]

Ms. CHESSNOE. The last thing I wanted to make is my——

Chairman MILLER. A lot of people in the audience want to testify. Obviously we cannot accommodate everyone. We are fully prepared to leave the record open so that people who want to comment on what they have heard this morning, or suggest questions for future hearings, will get an opportunity. I would hope the audience and others concerned with this issue would understand that. Go ahead.

Ms. CHESSNOE. Thank you. To continue, as the president of our organization here in northern Virginia, I can also say to you, I do not know of one case, of all our members, who have requested any type of payment. Never has there been an issue addressing liability.

I am at a loss and we are saying, "why us?"

Mr. **Coats**. I certainly do not mean to question whether or not you have done the right thing in terms of following up the insurance company. I guess we are all frustrated and trying to get answers as to what the problem is. I think perhaps the answer to that is not to ask you but to have the insurance companies come before us, testify before us and tell us what is the problem. Why are the rates going up? Why are you canceling the insurance? It occurs to me that Mr. Gejdenson and Ms. Johnson are better positioned to ask those questions than I am.

Mr. **Gejdenson**. Not all insurance companies in Connecticut. We will certainly talk to the ones in Connecticut.

Mr. **Coats**. I thought they were all in Connecticut.

Mr. **Gejdenson**. We would like them all to be in Connecticut, but we do not have quite all of them.

Mr. **Coats**. And it occurs to me, Mr. Chairman, that we are just in the opening round here. We have more work to do in this regard. Hopefully, we can schedule, as soon as possible, a hearing where we can get that information; and I want to yield back to——

Chairman **Miller**. Dr. Rowland?

Dr. **Rowland**. Thank you Mr. Chairman. I do not have any questions here but I will have some questions for the next panel.

Chairman **Miller**. Thank you.

Ms. **Gellert**. Mr. Chairman I would like to answer Mr. Coats' question from before when he said, "Have you contacted your agent?"

I have been called by numerous providers across the country over the last 2 months—to the point where my daughter hates to answer the telephone, she says she wants to charge me secretarial fees—because they all say they tried to call the insurance agent and the number is always busy. It is either that BMF is getting an awful lot of phone calls or they have taken their phones off the hook. I am not sure which but I have had numerous complaints from providers saying, "We cannot get a hold of the insurance agent to ask the question, why are we being canceled."

Mr. **Coats**. What is BMF?

Ms. **Gellert**. BMF Marketing is the agent that sponsors Mission Insurance Co. for family day care providers.

Ms. **Solon**. Mission sent us an important notice answering the question which is why I did not bother calling them. The important notice starts, first sentence, "adverse publicity in the care industry has been scaring insurance companies throughout the country."

Now if that is their notice to me, I figure they are the ones that are looking for insurance for us. They are the ones that have talked to all the insurance companies so that must be the answer and what am I going to do with a lowly provider in Falls Church, VA, and why bother to call?

Chairman **Miller**. Mrs. Johnson?

Mrs. **Johnson**. I would just like to say that I have asked the insurance companies on behalf of some of my providers exactly that question, and their answer to me is, "we simply are not in that market anymore." They are not in that market anymore because of the problems in pollution liability and malpractice and a number of other areas. All they needed to pull out of the market was a few national articles on sexual abuse. We are up against a wall. I hope that through this series of hearings we can get them to come before us and document how many cases they have ever had to pay. I hope we can separate this issue from the other greater liability issues.

I would say to my colleagues that if we fail to deal with some of the liability issues in the Superfund reauthorization bill, we will never be able to protect people like you from what that industry is suffering as a result of broad exposure by laws passed by this body. It is part of a larger very difficult problem which we have got to deal with in other arenas, or we will never be able to deal with it in this arena.

I would remind you that this issue is not unrelated to what we are doing in Superfund. We must deal with liability exposure in all areas. Municipalities in my district are suffering rate increases of 300 percent in their municipal liability.

When communities are faced with that in the public arena, the least of these insurance companies' concerns is the day care providers, unfortunately. We are going to have to do something about that because it is necessary that you have liability insurance or you will not be able to provide child care services. You have been caught up exactly in the wave of concerns and the litigious environment that legislation has, frankly, encouraged in America. This is the end result of, in my estimation, insufficiently, precisely-crafted legislation at a number of levels of Government the past couple of decades.

Now is the time of reckoning, and you are a part of it. I hope that we are able to help you, as well as municipalities, with insurance.

Chairman MILLER. Congressman Monson?

Mr. MONSON. No.

Chairman MILLER. Congressman Wheat.

Mr. WHEAT. No.

Chairman MILLER. In my meetings with representatives of the insurance industry, it was suggested that insurance would be provided, or is being provided to Child Care Programs that are sort of an adjunct to a larger facility—those that are sponsored by churches, those that are sponsored by the YWCA and YMCA.

Your testimony, however, Ms. Weaver, suggests that you are not immune from what is being experienced by family day care providers or from center based providers that are not associated with a larger institution——

Ms. WEAVER. You are correct.

Chairman MILLER. Your attachment shows that day care at the "Y" receives the same kind of treatment. You clearly have a larger pool of resources to draw from to pay that premium because you have a variety of sources of income.

Nevertheless, they went through your insurance policy much in the same fashion.

Ms. WEAVER. Exactly. We do have a wider resource to draw from but you have to remember the clientele we serve who cannot afford to pay——

Chairman MILLER. We have looked upon the "Y" as a major resource in terms of providing after-school care. They have come into the communities that I represent and offered to setup after school programs for what we have termed "latch-key children." Have you heard of what impact this is having on those programs?

Ms. **Weaver**. What we are looking at is either of two things. We either are going to have to close our doors to some of those centers, and by the way we do have five after school programs as well as 11 day care centers. Some of our day centers, in conjunction with day care, we also have after school programs.

We are going to perhaps have to just close down some of our programs.

Chairman **Miller**. Deborah, do you know if that is true in——

Ms. **Phillips**. I have not talked specifically to school age programs. I have talked to programs that bring in some school age children along with other age children.

But with respect to your earlier comment, within the Head Start community, we are hearing that the Head Start Programs that have been encompassed within CAP agencies have not been hit as hard yet as the independent Head Start Programs.

However, we are hearing that now the insurance companies are going back to the CAP agencies and asking if they include a Head Start Program or a Day Care Program under their auspices and are probably going to come back in September and look specifically at that portion of their services.

So I think what you suspect will happen is exactly true. It is confirmed by what we are hearing.

Chairman **Miller**. Thank you for your testimony. Hopefully while this hearing is only a beginning, it will rapidly lead to some positive conclusions. The picture that you paint and that has been painted elsewhere is that we seem to abide by the withdrawal of coverage, for whatever the reasons. Even if we should find out that the reasons are rational and justified, however it is clear from the testimony of this panel that the failure to have coverage puts providers in an unacceptable position.

Sometimes people make a decision, as many drivers do, that they will go uninsured. They decide they will expose themselves and the public at large. But I think that as Ms. Solon pointed out, that is unacceptable to you and to the people that would leave their children with you.

What appears to be happening here is that we basically are withdrawing one of the underpinnings of the social service network in this country. As Congressman Fiorio pointed out, with regard to midwives, as Congressman Gejdenson pointed out, with regard to Head Start, foster care, the YWCA, after school programs, infant programs, support is being withdrawn. Yet we have spent a year on this subject and with the support of every member of this committee have documented that child care is an absolute necessity for many working families, and yet we see that those people who have come forward in our society to provide the service are simply having the pins cut out from underneath them.

That clearly is unacceptable. I do not say that in an accusatory fashion. But it is obviously a situation that distresses those of us in public policy. The option, if that would happen, would be to revert to a federally run system of child care, I do not know how else to handle the situation, because the children are not going to go away if providers close their doors. The parents are not going to be relieved of the need for child care.

Ms. **Weaver**. Mr. Miller you also need to know that in order for these programs to operate, you must have a license. In order to have a license you must have some form of liability insurance.

Chairman **Miller**. I understand that. And, if you are running programs that participate with a Federal component—where there is a child care feeding program or title XX moneys, you are in violation of the law without a license. Congressman Gejdenson?

Mr. **Gejdenson**. Thank you Mr. Chairman. Let me just, in defense of my State, say that it has not yet been proven that the culprits are Connecticut-based. I think in the testimony that you heard that most of the people who have had their problems have had them with companies not based in Connecticut. It is my understanding that Aetna is still in the business. It to some degree reminds me of a story when I was in the judiciary committee in the State house. We were looking at product liability legislation and a representative of industry came before the committee and told us of a horrid story where a judge had awarded a multimillion dollar settlement to a gentleman who had used his lawnmower to trim his hedges. He said these two neighbors bought a lawnmower and each one grabbed hold of a wheel and they walked along the hedge, triming the hedge. The lawnmower slipped and cut off one guy's arms. They went to court under product liability and won millions of dollars. We were all astounded at the terrible judge who had given such an outrageous award for what was clearly a ludicrous use of a lawnmower.

Almost as an after thought at that hearing, I asked the witness to get us some information on that case. He came up with a trade journal that had the story and I said, "no, I wanted to see the actual court case or a report in the newspaper with the court case in it."

All of a sudden, that story disappeared and I certainly hope that we are not dealing with just the headlines in some papers about what is clearly a problem that we are all concerned about causing industries to drop your services.

Let me get a sense of what has happened in the last 10 or 12 years. If you can remember, how much have your rates gone up? If you cannot give it to us today, maybe you can give it to us in writing afterward. What has happened—maybe what has happened here is the industry was asleep at the switch, doubtful but maybe they have been charging you too little and now all of a sudden with some problems out there, they are trying to make up for lost time.

Ms. **Chessnoe**. I can address this from—not as far back as you say. Our organization, Northern Virginia Family Day Care Association, was founded in 1976. For approximately 2 years, there was much negotiation from our organization, with the insurance company.

At that time, insurance was literally unavailable and basically, IPA, the company before BMF, was the forerunner in offering this.

At that particular time I believe our first coverage was maybe $65 and we are talking about 1978.

Mr. **Gejdenson**. For liability?

Ms. **Chessnoe**. Liability, yes. Also, attached to liability has always been an accident policy.

Mr. **Gejdenson**. Stitches and what have you?

Ms. **Chessnoe**. Right, and those two have gone together at the minimum coverage which was offered. From that time we have had very very few raises as you can see and as I told you in my testimony, December 31, 1984 we could still get insurance at $82 per year.

From that point you see, it went up to $165 before it was cancelled, in a 6-month period.

Mr. **Gejdenson**. It went from, basically, between $60 and $80 over a how long a period of time? Five years?

Ms. **Weaver**. From 1978 to 1984.

Mr. **Gejdenson**. All right so 6 years they were in that range?

Ms. **Weaver**. That is correct.

Mr. **Gejdenson**. And then they got out of the market after doubling the premium.

Ms. **Gellert**. I would like to answer this also. We have established over—since about 1978, that would be the appropriate time—for a number of years the rates for family day care the insurance averaged somewhere between $85 and $120 per year for up until, I guess last year, and at the same time a rider on the homeowner, usually, which was restricted to three children, averaged $50 to $60 per year, OK?

A business rider, which is different from a child care rider on an insurance, was averaging $400 to 500 per year.

Mr. **Gejdenson**. So if you had a small company and provided day care services, that is your company?

Ms. **Gellert**. Right, and now the same services are averaging $800 per year. Or, not available.

Mr. **Gejdenson**. Let me ask you one last question. You represent what, two or three States here?

Ms. **Weaver**. Yes.

Mr. **Gejdenson**. Do you any of you know of major settlements dealing with child abuse, sexual abuse in any of your States? Any settlements at all, any cases?

Ms. **Weaver**. No.

Mr. **Gejdenson**. Thank you.

Chairman **Miller**. Congresswoman Johnson?

Mrs. **Johnson**. Yes, let me just say that I think companies are pulling out because they are afraid of what the liability might become. The reason companies are pulling out completely of providing insurance for example to small towns and municipalities to cover their solid waste disposal sites is because those companies no longer know what they are going to be liable for. In a court case last year former clauses that limited their liability for things that they did not want to take responsibility for were invalidated.

Because of this court ruling, former, limiting clauses will not be recognized in terms of future liabilities. The insurance companies are finding themselves liable for incidents that they did not collect premiums to cover.

I would ask all of you to draw up, for me, what you need as basic coverage.

In other words, do you need coverage for a child who falls and breaks its arm, if they pull over a pan on the stove and get hurt, and so on. What would be the possibility of having insurance that would exclude a certain kind of problem like sexual abuse? I do not know whether we want to entertain that possibility or not, but I think we should begin to look at what the ordinary coverage is that is critical to your operation.

Can we circumscribe that liability so that parents who leave their children with you know that they will have liability up to *x* amount of dollars, and above that, their own personal insurance should cover the accident—the exposure of that child in whatever setting.

This is common in school situations. Often we do not pick up the school insurance offered throughout the public school system because our own insurance is superior.

What we need to look at, to some extent, is the nitty-gritty reality of the interface of individual insurance that many families have through their employer and the exposure of their child in your day care setting and exactly what you need for licensure.

If you could begin to work with me on those details, I can begin to work with you and the insurance companies. I see where we can find that product that we absolutely must have on the market at a reasonable and affordable price.

I honestly do believe that clarifying the risk that the company is taking is absolutely essential to not only an affordable price, but even to getting the product back on the market. It is a very similar problem to that we are having with the municipalities with malpractice, and with product liability. We are approaching the same kind of crisis in all of those arenas.

Let us just try this approach. It will our thinking and perhaps provide some information that we do not have now. Please get back to me as to those details.

Chairman MILLER. Mr. Smith?

Mr. SMITH. Thank you, Mr. Chairman. I apologize for having to leave the room for a few minutes. I am not sure if this question was asked; but, what, in your opinion, is the answer—what has to be done? Do we have to simply find a financial way, a combination of all of this from the Congress to the insurance companies, that it pays to pay these high, exhorbitant costs? Do we have to set some parameters on legal suits? What is the answer in your opinion; what do we have to do?

We obviously have to be protected—you have to be protected, that is for sure, if you are going to operate. What is the answer? What do you suggest that we should do?

Ms. SOLON. Well it does not help to ask you to pay for something that they will not offer us.

Mr. SMITH. Well, I do not think that is true, but they are not offering it because they feel they cannot afford to offer it, I suppose. But still, what is the answer? You have to have insurance. What are you asking us to do?

Ms. PHILLIPS. I think that what you are doing right now is extremely important, which is to try to get to the bottom of the problem, to try to understand the real impact for child care providers and children and families. You and Representative Gejdenson have commissioned the GAO report, I would like to see that speeded along as quickly as possible.

I would like to see reports from that made public as soon as they emerge rather than wait for the final GAO report to be issued.

I would also ask you to come back and talk to us again in September when you reconvene because we are hearing that this crisis is going to get much worse in August and September, before it gets better. So to get an accurate estimate of the magnitude of the problem, I think we are going to have to come back and inform you in a couple of months. And I would like to have the opportunity to do that.

Mr. SMITH. Sure.

Ms. WEAVER. Could I answer that question also. What we would like to see so far as the YWCA, as well as the day care directors organization that I represent today, is some type of cap. What we are afraid of is if our insurance increases this drastic this year, what is going to happen in 1987, what is going to happen in 1988, what is going to happen in 1989?

What we foresee is ourselves completely out of business if there is not some type of cap on the insurance rates.

Mr. SMITH. To the best of your knowledge, is the same thing happening with other groups who are also in some way minding children, for example, camps, school districts——

Ms. WEAVER. It is my understanding that the same thing is happening nationwide, anywhere where you have people involved with the livelihood of children. It is just not a local problem. It is a national problem.

Most people are just—agencies and centers—are just biting the bullet and finding monies from somewhere, cutting back on other things to pay for the insurance prices because they need insurance and they are just not complaining about it. Some of them are.

Mr. SMITH. You feel that the carriers are getting to the point where they may not provide liability insurance for school districts, boys and girls camps?

Ms. WEAVER. Sure. In Baltimore, MD, I know that is the case because the mayor of Baltimore is currently meeting with all the insurance executives around the whole State of Maryland as to why their insurance rates have increased also.

So this is just not a center—day care center—problem, it is a problem nationwide, wherever children are involved.

Mr. SMITH. Thank you.

Chairman MILLER. Thank you very much for your help. We expect to be in continued touch with you.

The second panel the committee will hear from is made up of Mr. Jim Chastain, who is a professor of insurance at Howard University and director for Center Insurance Education, Washington, DC; Joseph Silverman, who is the executive vice president of BMF Marketing Insurance Services from Sherman Oaks, CA; and Georgia D. Yocum, who is the chief executive officer of Loma Rica Insurance Agency in Grass Valley, CA.

Your written testimony will be made a part of the permanent record in its entirety and to the extent that you can summarize, we will appreciate it.

We will hear first from Mr. Chastain.

STATEMENT OF JAMES CHASTAIN, PROFESSOR OF INSURANCE, HOWARD UNIVERSITY, DIRECTOR, CENTER FOR INSURANCE EDUCATION, WASHINGTON, DC

Mr. CHASTAIN. My name is James Chastain; but, after hearing the testimony I have heard for the last hour, I think it might better be changed to Daniel.

I am employed as a professor of insurance and director of the Center for Insurance Education at Howard University.

I have been an insurance educator for 33 years. I served as dean of the American Institute for Property and Liability Underwriters. For 6 years, I served as the educational consultant to the Conference of Insurance Legislators, and recently I served as chairman of the Steering Committee for implementation of the District's no-fault automobile insurance law.

My comments today are entirely personal, made at the request of the committee staff. It is my understanding, reinforced this morning, that a problem exists regarding the availability and affordability of liability insurance covering child care facilities.

Similar problems have occurred at other times with respect to flood insurance, fire and theft insurance in the inner city, automobile insurance for high risk drivers, medical malpractice insurance, products liability insurance, life insurance for military personnel, municipal liability insurance, and surety bonds for minority contractors, to name a few.

These problems have been resolved in various ways over the years. Sometimes with, and sometimes without, government action. Some of the factors probably relate to the current problem of child care insurance are as follows:

Nobody in the insurance industry has told me that these are the reasons for the problem; but, as an observer, it seems to me that they are probably important.

First of all, with regard to the current insurance climate, there are more than 3,400 companies who write some kind of property and liability insurance. The vast majority of insurance is written by about 900 companies which belong to about 100 groups of companies.

These 100 groups compete fiercely for market share. There is a common misconception, I think, that all insurance companies work together, but it is my impression that there are various factions in the insurance business that would like nothing better than do other factions in.

The companies use a variety of marketing systems and financial structures. They compete not only against themselves, but against off-shore companies and against various self-insurance and risk retention plans that various companies have.

The lack of concentration of the insurance market, such as exists in many other manufacturing-type of operations, among a few insurers is probably responsible for the radical swings and insurance price and availability known as the underwriting cycle.

At the top of the underwriting cycle, prices are high, underwriting is moderately tough producing good profit to companies.

The last top of the underwriting cycle occurred in 1977 and 1978. This encourages new capital into the insurance business. It encourages looser underwriting because companies want to get the premiums and it encourages reduced rates.

Profits decline. This part of the cycle then produces rate wars and so-called cash-flow underwriting, the name given to loose underwriting practices.

Underwriting losses develop but may persist for several years when offset by investment gains. This part of the most recent underwriting cycle lasted from 1978 to 1983. It was lengthened by high interest rates during that period of time and a rapidly rising stock market.

During this period agents told many horror stories to them of accounts that had been paying $80,000 last year, being quoted by the agent this year at $60,000 and lost to a competitor for $40,000.

The turning point in this underwriting cycle occurs only when company executives become alarmed by financial failure of some other company or when there is unrest among the stockholders or other owners of the companies or when the reinsurance market reflects this by being tightened.

All of these things occured by late 1983. In 1984 companies began to raise prices radically and to restrict underwriting, not because they were following a price leader but because they were threatened with extinction.

This trend is likely to continue for another 2 or 3 years. The doubling of prices for some insurance this year is returning to the prices of the 1977-78 level.

The increased prices and restrictive underwriting are not unique to child care facilities. They exist for virtually all personal and commercial lines of insurance.

Just last week, for example, the leading writer of substandard automobile insurance in the District of Columbia announced plans to cease all writing here.

Some agents have told me that companies are declining all new business from them at present. The table included in my statement shows the extent of industry losses in the line marked net underwriting gain or loss.

You will note that in 1981 this figure was $6 billion, in 1982 $10 billion and in 1983 $13 billion. The loss was greater than that in 1984.

As premiums rise today, it will probably take another year or two for these premium rises to show up in these figures because there is a lag.

The second factor involving the insurance market today has to do with bad liability insurance experience. Child care liability insurance is included in general liability statistics.

There are some statistical material which shows that general liability insurance has been worse, substantially, than the average of all property and liability insurance over the past 3 years.

In attempting to regain a profitable position, it is not surprising that companies are focusing attention on all general liability lines.

The third factor, which is important in this issue, I believe, is generally called the long tail. When liability insurance is written on an occurrence basis, for example, for losses that occur during 1985, the insurer may be responsible for a loss litigated many years after the policy date.

Some types of liability insurance have longer tails than others so that this litigation can occur much later. Malpractice—medical malpractice insurance has a long tail. Products liability insurance, especially asbestos cases that may date all the way back to 1940, has a long tail. Insurers are aware of the special long tail problem involved in losses involving young children.

For example, losses from a physical abuse may go undetected for years, or the child may sue years after receiving the child care upon becoming an adult.

Years of bad experience in medical malpractice and products liability insurance have made underwritings wary of any type of insurance with a long tail.

The fourth factor that I see as important is the nature of the child care exposure. My impression is that the child care business has grown rapidly and haphazardly in the last 20 years.

Facilities range from large franchised operations to home basements converted for the care of two or three children.

The quality of staff may vary radically from facility to facility, and from time to time. State standards also vary widely.

In such a situation underwriters may need some time to learn to sort out good from bad risks, and they may be going through that period now.

I would classify, on the basis of these four factors that I have been talking about, the present child care insurance market situation is more of a problem than a crisis.

The phase of the underwriting cycle likely to emerge in the next 2 or 3 years, following the present phase, will improve the situation greatly when companies can get the rates up to the point where they begin scrambling for business again.

However, it is still true that we are all dead in the long run. An improvement likely to occur in 2 or 3 years does not satisfy the child care business owner with an immediate problem of availability or affordability for liability insurance.

Because of the complexity of the child care business, I do not believe there is a quick fix to the problem. However, I believe that some actions could help to reduce the problems.

We have talked this morning about the importance of better communications between insurers and child care businesses. I believe that can help. This hearing can help. The next one to be held later can help.

A study of the nature and extent of child care exposures followed by a conference between underwriters and child care business managers could help.

A communications network, coordinated by State insurance departments to put child care businesses with insurance market problems in touch with interested underwriters might help.

Such a network was established several years ago to deal with the somewhat similar problem in products liability insurance.

A study of the nature and extent of child care business insured losses would be helpful both to the underwriters, in distinguishing between good and bad exposures, and to child care business owners to aid them in more effective loss control actions.

What we are seeing now in child care is something that we have been through several times before in products liability and medical malpractice, where following a market crisis, there was great emphasis on loss control activity by the insurers.

There probably needs to be more work on loss control at the child care center. One other modest action might be considered—to amend the Risk Retention Act of 1981 to include child care businesses.

This act was passed to help with the rapidly rising cost and reported unavailability of products liability insurance.

The law created alternatives to traditional commercial insurance by making it easier to self-insure through risk retention groups and permitting the purchase and sale of group insurance. It is my understanding that that act has been helpful and is expected to be substantially more helpful in the acquisition of products and risk solutions than it has been in the past because of the current market crunch.

In summary, I believe that more information, better communication, time itself, and perhaps some group insurance and risk retention groups legal—making them legal is all that is needed to deal with the current child care insurance problem.

[Prepared statement of James Chastain follows:]

PREPARED STATEMENT OF JAMES CHASTAIN, PROFESSOR OF INSURANCE AND DIRECTOR OF THE CENTER FOR INSURANCE EDUCATION AT HOWARD UNIVERSITY

My name is James J. Chastain. I am employed as Professor of Insurance and Director of the Center for Insurance Education at Howard University. I have been an insurance educator for 33 years and served as Dean of The American Institute for Property and Liability Underwriters, the organization granting the professional designation Chartered Property and Casualty Underwriter. For six years I served as educational consultant to the Conference of Insurance Legislators, and recently served as Chairman of the Steering Committee for implementation of the District of Columbia's No Fault Automobile Insurance law. My comments are entirely personal, made at the request of the committee staff.

It is my understanding that a problem exists regarding the availability and affordability of liability insurance covering child care facilities. Similar problems have occurred at other times with respect to flood insurance fire and theft insurance in the inner city, automobile insurance for high risk drivers, medical malpractice insurance, products liability insurance, life insurance for military personnel, municipal liability insurance, and surety bonds for minority contractors. These problems have been resolved in various ways with and without government action.

Some factors probably related to the current problem of child care insurance are as follows:

1. CURRENT INSURANCE CLIMATE

More than 3,400 companies write some forms of property or liability insurance, but the vast majority is written by about 900 companies operating in all or most states. Most of the 900 companies are parts of about 100 "groups" which compete fiercely for market share. The companies use a variety of marketing systems, and financial structures, and compete not only against themselves but against off-shore companies and self-insurance and risk retention plans. The lack of concentration of the insurance market among a few insurers is probably responsible for the radical swings in insurance price and availability known as "the underwriting cycle".

At the top of the cycle prices are high, underwriting is moderate producing good profit. The last top of the underwriting cycle occurred in 1977-78. This encourages new capital into the business, looser underwriting, and reduced rates. Profits decline. This part of the cycle produces "rate wars" and "cash flow underwriting," the name given to loose underwriting. Underwriting losses develop but may persist for several years when offset by investment gains. This part of the most recent underwriting cycle lasted from 1978 to 1983, lengthened by high interest rates and a rising stock market. During this period agents told horror stories of accounts paying $80,000 last year, being quoted by the agent this year at $60,000 and lost to a competitor with a rate of $40,000.

The turning point in the cycle occurs only when company executives become alarmed by financial failure of some other companies, when there is unrest among the owners of the company or when the reinsurance market tightens. This occurred in late 1983. In 1984 companies began to raise prices and restrict underwriting. This trend is likely to continue for another two or three years. The doubling of prices for some insurance this year is returning of prices to the 1977-78 level.

The increased prices and restrictive underwriting are not unique to child care facilities. They exist for virtually all personal and commercial lines of insurance. Just last week, for example, the leading writer of sub-standard automobile insurance in the District announced plans to cease all writing here. Some agents have told me that companies are declining all new business at present.

The Table below shows the extent of industry losses in the line Net Underwriting Gain (Loss). The loss in 1984 was greater than 1983 because there is a lag between premium increases and improved financial figures.

Operating Results, Property/Casualty Insurers, 1981-1983
(000 Omitted From Dollar Figures)

	1983	1982	1981	% Change 1982-83	% Change 1981-82
Assets	$249 121 282	$231 692 713	$21[illegible] 302 742	+ 7.5%	+ 9.1%
Net Premiums Written	108 982 808	103 968 221	99 275 575	+ 4.8	+ 4.7
Premiums Earned	106 966 586	102 005 305	97 465 271	+ 4.9	+ 10.5
Losses and Adjustment Expenses Incurred	87 206 936	81 366 925	74 941 996	+ 7.2	+ 8.7
Loss and Loss Adjustment Ratio	81.53%	79.77%	76.79%	+ [illegible]	+ 3.9
Underwriting Expenses Incurred	30 475 221	29 145 197	27 [illegible]	+ 4.5	+ 5.9
Underwriting Expense Ratio	28.39%	27.44%	27.36%	+ 1.4	+ 2.1
Combined Ratio (before Dividends to Policyholders)	109.91%	107.75%	104.12%	+ 2.1	+ 3.4
Combined Ratio (after Dividends to Policyholders)	111.98%	109.55%	106.21%	+ 2.2	+ 3.3
Statutory Underwriting Gain (Loss)	$(11 287 953)	$(8 303 239)	$(4 463 988)	− 33.5*	− 86.0*
Dividends to Policyholders	2 214 117	1 986 427	1 823 748	+ 12.8	+ 8.9
Net Underwriting Gain (Loss)	$(13 322 070)	$(10 289 666)	$(6 287 636)	− 29.5**	− 63.7**
Net Investment Income	15 973 234	14 906 655	13 248 [illegible]	+ 7.2	+ 12.5
Operating Earnings After Taxes	3 869 137	5 332 571	6 905 849	− 27.4	− 22.8
Policyholders' Surplus	65 [illegible]	60 394 591	53 904 789	+ 8.6	+ 12.[illegible]
Premium to Surplus Ratio	1.66 to 1	1.72 to 1	1.85 to 1		
Dividends to Stockholders	$ 3 001 185	$ 2 735 173	$ 2 394 106	+ 9.7	+ 14.2

[illegible]

Source: A.M. Best Company, Inc. Best's Aggregates & Averages.

--INSURANCE FACTS, 1984-85 PROPERTY/CASUALTY FACT BOOK, Insurance Information Institute, NY

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2. BAD LIABILITY INSURANCE EXPERIENCE.

Child care liability insurance is included in General Liability statistics. The Table below shows that General Liability Insurance has been worse (137.6% in 1983) than the average (109.9% in 1983) of all property/casualty insurance. In attempting to regain a profitable position it is not surprising that companies are focusing attention on General Liability.

Table 2

General Liability/Medical Malpractice, 1975-1983

	General Liability			Medical Malpractice		
Year	Premiums Written	Annual % Change	Combined Ratio*	Premiums Written	Annual % Change	Combined Ratio*
1975	$3 085 226 000		115.6	$ 895 425 000		117.7
1976	4 251 298 000	+37.8	106.5	1 132 790 000	+26.5	109.8
1977	5 845 075 000	+37.5	99.6	1 247 798 000	+10.2	92.9
1978	6 490 064 000	+11.0	96.9	1 215 789 000	− 2.6	102.6
1979	6 612 474 000	+ 1.9	97.6	1 204 326 000	− 0.9	112.6
1980	6 414 678 000	− 3.0	106.6	1 275 603 000	+ 5.9	128.2
1981	6 046 292 000	− 5.7	115.3	1 338 299 000	+ 4.9	135.7
1982	5 668 459 000	− 6.2	128.6	1 490 270 000	+11.4	149.3
1983	5 679 295 000	+ 0.2	137.6	1 568 007 000	+ 5.2	150.1

*After dividends to policyholders.

Source: A.M. Best Company, Inc., Best's Aggregates & Averages.

--INSURANCE FACTS, 1984-85 PROPERTY/CASUALTY FACT BOOK, P. 29, Insurance Information Institute, NY

3. THE LONG TAIL

When liability insurance is written on an "occurrence" basis the insurer may be responsible for a loss litigated many years after the policy date. Some types of liability insurance have longer tails than others. Medical malpractice insurance has a long tail. Products liability insurance (especially asbestos) has a long tail. Insurers are aware of the special "long tail" problem involved in losses to young children.

For example, losses from physical abuse may go undetected for years, or the child may sue years after receiving child care, upon becoming an adult. Years of bad experience in medical malpractice and products liability insurance have made underwriters wary of long tails.

4. NATURE OF THE CHILD CARE EXPOSURE

My impression is that the child care business has grown rapidly and haphazardly in the last twenty years. Facilities range from large franchised operations to home basements converted for care for two or three children.

The quality of staff may vary radically from facility to facility, and from time to time. State standards vary widely. In such a situation underwriters may need some time to learn to sort out good from bad risks.

I would classify the present child care insurance market situation more as a problem than as a crisis. The phase of the underwriting cycle likely to emerge in two or three years, following the present phase, will improve the situation greatly. However, it is still true that "we are all dead in the long run" and improvement likely to occur in two or three years does not satisfy the child care business owner with an immediate problem of availability or affordability of liability insurance.

Because of the complexity of the child care business I do not believe that a quick fix is possible. However, some actions could help reduce the problem.

Better communication between insurers and child care businesses can help. This hearing helps. A study of the nature of child care exposures followed by a conference for underwriters and child care business managers could help. A communications network coordinated by state insurance departments to put child care businesses with insurance market problems in touch with interested underwriters might help. Such a network was established several years ago to deal with the somewhat similar problem in products liability insurance.

A study of the nature and extent of child care business insured losses would be helpful both to underwriters, in distinguishing between good and bad exposures, and to child care business owners to aid them in more effective loss control actions.

One other modest action might be considered -- to amend the Risk Retention Act of 1981 to include child care businesses. This act was passed to help with the rapidly rising cost and reported unavailability of products liability insurance. The law created alternatives to traditional commercial insurance by making it easier to self-insure through risk retention groups and permitting the purchase and sale of group insurance. It is my understanding that the Act has been helpful.

In summary, I believe that more information, better communication, time and perhaps making group insurance and risk retention groups legal are all that is needed to deal with the current child care insurance problem.

STATEMENT OF JOSEPH S. SILVERMAN, EXECUTIVE VICE PRESIDENT, BMF MARKETING INSURANCE SERVICES, INC., SHERMAN OAKS, CA

Mr. SILVERMAN. I would like to extend my thanks to this committee for the opportunity of presenting testimony on the care provider insurance dilemma with the availability of professional liability insurance.

Earlier the panel was asked to come up—the first panel was asked to come up with the types of insurance that was needed. We have known for a long time the type of insurance that is needed by the day care community is professional liability but because of the definitions, it does not fit the court system of education, training, and development.

We have coined the phrase, negligent supervision and that is the crux of the majority of the claims that we have seen. This type of coverage was first made available in 1970 by a company that we acquired in 1982——

Since that time three companies have provided the coverage on a national basis. Two of them have canceled the program because premiums did not keep up with losses and the most recent cancellation was the result of the insurance company losing its reinsurance. Since the first of April, we have contacted and discussed the problem with over 50 insurance companies in the United States.

To date, only one of those companies has agreed to undertake writing family day care insurance and that company is limited to do business in the State of California.

In the other 49 States, we are still trying to solve the problem. I will not go into depth of the insurance availability for foster homes. I have elected to touch on the subject only because their liability exposures closely parallel that of family day care providers, and the combined adverse publicity of foster care, family day care and day care centers has contributed to the problems of categorizing these classes of business as high risks.

Periodicals received by our office generally agree that there are over 1 million family day care providers in the United States and the number is growing at an estimated 30 percent a year.

A true number is really not known but information from research such as the Senate Latch-key Report indicates that as much as 70 percent are unlicensed and unregulated, commonly referred to as underground homes.

Yet the majority of the current legislation occurring throughout the country is aimed at the law-abiding 30 percent who take pride in their professionalism. These regulations can include change in habitat structure, mandatory education, medical training such as CPR, communicable disease identification, first-aid and mandatory insurance.

With the recent enactment of mandatory insurance laws, large numbers of care providers have been seeking the availability of insurance after learning they are not covered by their homeowners policy.

Our research has shown that almost 75 percent of the people who have insurance for family day care homes have relied on their homeowner insurance and have now just found out that it does not cover negligent supervision.

Although much of the legislation is supported, there is a great concern that runaway legislation making demands which cause hardships on the care providers may force many care providers into the ranks of the underground homes.

Enforcement of licensing or registration remains less active due to manpower and budgets, and the penalties imposed are not adequate enough to cause concern of the unlicensed home provider.

The unlicensed provider is not hampered by many of the expenses and restrictions on the number of children and are able to take advantage of the acute shortage of day care facilities.

This it not to say they are not good providers. Only that the public does not have the advantage of regulated controls for health, criminal or safety violations.

Since 1984, more and more States, and in some cases cities, have either passed, introduced or are considering legislation making insurance mandatory.

To date, we know this to be the case in Arizona, California, Idaho, Illinois, Kansas, Massachusetts, Nevada, New Jersey, Pennsylvania, and throughout the military.

The care provider industry seems to have hit its zenith of public awareness in the past several years primarily due to the adverse publicity relating to child abuse and sexual molestation.

This publicity has been unfairly associated with care providers when department of social services and the care provider advocates are aware that there is research revealing that between 90 and 98 percent of these items that hit the news media occur in the child's own environment, not that of the care provider system.

The adverse publicity, the long period needed to discover losses, our existing tort system, high-legal expenses involved in insuring activities associated with minors has caused the insurance industry to place care providers in a high risk classification.

The insurance industry is trying to recover, as has been pointed out earlier, from several years of very high losses. Their losses have also impacted their ability to insure many risks due to the availability of their surplus.

Accordingly, they are raising insurance costs dramatically and are making business decisions not to insure many high risk classes of businesses. I might add that the availability of day care liability insurance has also impacted other lines of insurance involving family day care providers.

Some insurance companies have either cancelled or refused to write homeowner policies for people caring for children in their homes, in spite of the fact that that business pursuit is not covered nor do they provide the negligent supervision coverage.

It has happened with such frequency in the state of Washington that legislation has recently passed prohibiting the cancellation or refusal to write insurance because of day care activities.

Recent loss figures accumulated by our office has shown that over the last 7 or 8 years the insurance companies have incurred losses of almost $2 for every $1 they have taken in in premium.

These are hard figures and substantiated by the statistics that they have provided to us. Historically, there is a delay of several years in reporting losses.

One reason is the lack of urgency to meet a time restriction. Minors have until they reach their majority age before a claim must be filed.

Often it is many years before that claim is brought forward. It also a matter of not knowing that a claim exists or that one can be made.

This late reporting and development of losses has made future loss predictions and acturarial development extremely difficult for the foster and family day care risks.

In conclusion, I would like to state that our records indicate that the family day care home insurance program and that of the day care centers is an insurable risk at an affordable cost.

It is our belief that the claims activity for this class of business should not prohibit insurance companies from offering the insurance providing they can maintain a premium—an adequate premium level.

The problem has not been one of frequency. There are very very few claims that are filed throughout the country in proportion to the number of homes that are insured.

The problem is severity and when a claim does occur, the legal expenses and the settlement costs run into the tens of thousands of dollars.

If insurance is not available, many providers will go out of business, impacting an industry already facing a shortage of facilities.

If the cost is prohibitive, or if costs cannot be passed on to the consumer, it could effect the community at large in a number of ways. One would be increasing the number of latch-key children, which we already know has an impact on the police and fire department's costs, and another by increasing the welfare roles with those who have to quit work because they have no place to leave their children.

A recent development that has occurred in California that had hit the papers is that many families who cannot afford day care are starting to place their children, after school, in the public libraries, saying, "stay here until 7 until we come to pick you up."

The cost, again, is a matter of claims lag. The cost since 1978 has—that is on file with my testimony—shows that the rates have not kept up with the losses.

The coverage—we know what they need. It has to be negligent supervision. The insurance companies face the problem of unknown exposures.

The courts impose liability on the insurance system but the policies were not intended to cover. Another reason that was alluded to earlier is that they are running scared.

We see some of the solutions as Federal relief for those who cannot afford day care and the cost of it because of the increase in insurance costs.

We also see the need for higher tax deductibility for the people who use day care so that if the costs are passed on, they can afford them. Because if we do not and day care falls by the wayside, then the economy of this country is going to be greatly jeopardized by the loss of productivity and manhours of the working single parent.

Thank you.

Chairman **MILLER**. Thank you. Ms. Yocum?

[Prepared statement of Joseph Silverman follows:]

PREPARED STATEMENT OF JOSEPH S. SILVERMAN, EXECUTIVE VICE PRESIDENT AND CHIEF OPERATING OFFICER OF BMF MARKETING INSURANCE SERVICES, INC.

My name is Joseph S. Silverman. I am the executive vice president and chief operating officer of BMF Marketing Insurance Services, Inc., a California corporation and wholly-owned subsidiary of Bayly, Martin, and Fay International, Inc.

I would like to extend my thanks to this committee for the opportunity of presenting testimony on the care provider industry's dilemma with the availability of professional liability insurance.

I first became acquainted with our existing specialty insurance program for family day care homes, and foster parents, in the spring of 1981, just prior to our acquisition of another company who, in 1970, had originated a specially-designed policy insuring foster parents and family day care homes for their legal liability arising from negligent supervision.

This insurance was first made available through the Hartford Insurance Co., where it was offered for approximately six years, until the program was cancelled because premiums were inadequate to cover losses.

In 1977, National Union Insurance, Co. of Pittsburg, PA began to underwrite the program until August 1, 1983, when they also elected to discontinue providing cover due to inadequate premiums to cover losses.

In August 1983, Mission Insurance Co. became the underwriter for these programs. In 1985, they lost their reinsurance and processed cancellation notices July 1, 1985 on all the programs nationwide.

I was personally involved in the accumulation of claims statistics for replacement of the insurance programs, both after National Union decided to discontinue this class of business in 1983, and again in 1985, when the Mission Insurance Co. cancelled.

The difficulty in finding another insurance company in 1983 was not as pronounced as the more recent attempt in 1985. To date, we have contacted over 50 companies, and as of today, we have found only one company willing to offer the insurance for the family day care liability program. Unfortunately, they are permitted to do business in California only and cannot offer coverage in the other States.

My testimony today will be confined to insurance availability and claims information for foster parents and family day care homes. The loss information developed from approximately 1977 to the present will be broken down into two categories; foster parents, and family day care homes.

I will not go into depth on the insurance availability for foster homes, as the impact is not presently affecting a significantly large part of the foster parent population.

I have elected to touch on the subject only because their liability exposures closely parallels that of family day care providers, and the combined adverse publicity of foster care, family day care, and day care centers has contributed to the problems of categorizing these classes of business as high risks.

Insurance, with some minor exceptions, is made available to the foster parents either by a State, county, city, or one of their designated agencies. It is either purchased in the form of a separate policy or included in their insured or self-insured programs.

It is important to note that there is no constant on the number of homes or children. There is a high attrition rate among foster parents and frequent turnover in children.

Although most foster parents are licensed for a maximum of six children at any one time, a foster home could care for a greater number during a 1-year term, depending on the turnover, which is controlled by those agencies making the placements.

The profile of the foster parent has changed. Over the past few years, local governments budgetary problems, coupled with changes in social ideology has taken delinquents, physic, and/or mentally handicapped, and troubled teenagers out of institutions and placed them in foster homes.

It is also necessary to review circumstances which are changing the profile of the care provider. This office works closely with the National Family Day Care Associations. Most of the State and local associations, advocacy groups such as the Children's Foundation in Washington, DC, as well as resource and referral agencies throughout the country. We are in constant touch with care providers, both through daily contact and through workshops and conferences.

Periodicals received by our office generally agree that there are over 1 million family day care providers in the United States and that the number is growing at estimates of 30 percent per year.

A more exact number is not known. Information from research, such as the Senate latch-key report, indicate that as much as 70 percent are unlicensed and unregulated, commonly referred to as "underground homes", yet the majority of the current legislation occurring throughout the country is aimed at the law-abiding 30 percent who take pride in their professionalism.

These regulations can include change in habitat structure, mandatory education, medical training; such as, CPR, communicable disease identification, first aid, and mandatory insurance.

The greater percentage of family day care providers have erroneously relied upon the homeowners insurance to provide coverage for their day care activities, or elected not to buy insurance.

With the recent enactment of mandatory insurance laws, large numbers of care providers have been seeking the availability of insurance after learning they are not covered by their homeowners policy.

Although much of the legislation is supported, there is a great concern that runaway legislation making demands which cause hardships on the care provider may force many care providers into the ranks of the underground homes. Enforcement of licensing or registration remains less active due to manpower and budgets, and the penalties imposed are not adequate enough to cause concern of the unlicensed home provider.

The unlicensed provider thrives because they are not hampered by many of the expenses or restrictions on the number of children, and are able to take advantage of the active shortage of day care facilities.

This is not to say they are not good providers, only that the public does not have the advantage of regulating controls for health, criminal or safety violations, to name a few.

Since 1984, more and more States, and in some cases cities, have either passed, introduced or are considering legislation making insurance mandatory. To date, we know this to be the case in Arizona, California, Idaho, Illinois, Kansas, Massachusetts, Nevada, New Jersey and Pennsylvania.

The care provider industry seems to have hit its zenith of public awareness in the past several years because of all the adverse publicity relating to child abuse and sexual molestation.

This publicity has been unfairly associated with care providers when departments of social services and the care provider advocates are aware that there is research revealed that between 90 to 98 percent of these items that hit the news media occur in the child's own environment, not that of the care provider. The adverse publicity, the long period needed to discover losses, the tort system, and high legal expenses involved with insuring activities associated with minors has caused the insurance industry to place care providers in a high risk classification.

The insurance industry is trying to recover from several years of huge losses. These losses have impacted their ability to insure many risks due to their available surplus.

Accordingly, they are raising insurance costs dramatically and are making business decisions not to insure many high risk classes of business.

This has also impacted other lines of insurance involving family day care providers. Some insurance companies have either cancelled or refused to write homeowner policies for people caring for children in their homes, in spite of the fact that business pursuit is not covered under the policy.

It happened with such frequency in the State of Washington that legislation was recently passed prohibiting the cancellation or refusal to write insurance because of day care activities.

Before commenting on premium and loss statistics, I wish to express that the information contained here is specific to programs developed and offered only by our office. I wish to state I am not degreed, do not hold any professionally-designated classifications nor do I have any formal actuarial training. However, 16 of my 21 years in the insurance business have been with two of the largest insurance brokerages firms in the country developing and administering insurance for trade groups and associations.

Testimony dealing with statistical loss information is based on information provided to our office by the aforementioned National Union and Mission Insurance Cos. We do not have any experience associated with the Hartford Insurance Co. experience prior to 1978.

From 1977 to 1983, we have insured accumulatively almost 300,000 foster homes of various classifications. This represents an estimated 1.2 million children during this period of time. An average of 50,000 homes and 200,000 children per year.

Foster homes written during this period have developed claims to date totalling $2,590,940 incurred losses. Incurred losses are made up of paid losses, legal and investigating expenses, and reserves on reported claims which have not been settled.

Claims analysis of the larger foster and day care homes reveal the following frequency and size of claims:

Size range	Foster Parent Claims	Family Day Care Claims
$10,000 to $25,000	27	14
$25,001 to $50,000	7	5
$50,001 to $100,000	12	10
$100,001 to $150,000	2	2
$151,001 to $200,000	1	0
$200,001 to $300,000	0	1
Largest	$175,000	$500,000

Losses combined with estimated insurance company operating costs indicate the cost to date for each premium dollar has been $1.20 for a foster home, and $1.86 for a family day care home, or stated in loss percentages to income, 120 percent and 186 percent respectively.

These figures do not take into consideration the additional cost of claims not yet reported, or the full development of reported claims still open.

Historically, there is a delay of several years in reporting losses. One reason is the lack of urgency to meet a time restriction. Minors have until they reach their majority age before a claim must be filed. Often it's just a matter of not knowing a claim exists or that one can be made.

This late reporting and development of losses has made future loss predictions and actuarial development extremely difficult for foster and family day care risks.

During the term in review, premiums did not keep pace with losses. The average annual premium for a foster home for $300,000 liability insurance was $11.00 until 1982; $15.00 in 1983; and $25.00 in 1984 and 1985.

There was also little premium change during this term for family day care. The average per home annual premium for $300,000 liability was $46.00 from 1978-1980; $66.00 from 1981-1982; and $80.00 from August 1983 to April 1985. Before cancellation of the Mission program, it went to $160.00.

As of July 15, 1985, the minimum cost is $445.00 which includes a $30.00 association membership credit.

In conclusion, it is our belief that the claims activity for this class of business should not prohibit insurance companies from offering the insurance, providing they can maintain an adequate premium level.

If the insurance is not available, many providers will go out of business, impacting an industry already facing a shortage of facilities.

If the cost is prohibitive, or if costs cannot be passed on to the consumer, it could effect the community at large in several ways; one, by increasing the number of latch-key children, which has an impact on the police and fire department's costs, and two, by increasing the welfare roles with those who would have to quit working because they have no place to leave their children.

STATEMENT OF GEORGIA D. YOCUM, CHIEF EXECUTIVE OFFICER, LOMA RICA INSURANCE AGENCY, GRASS VALLEY, CA

Ms. YOCUM. Thank you for inviting me. I have learned an awful lot today. I was asked to share my views and I am going to quickly go over some things that have already been said.

First I would like to address the fact that the people who we have literally lost the market for or did for a short while were the day care homes. That is one child to 12 children.

I still have many markets open for day care centers but the rates, of course, are considerably higher. The reason that the markets have not closed completely on the day care centers is because they can obtain a higher premium for their exposure. One to 12 children—we are under $1,000 and that really is a very very small premium for their exposure.

My main thrust is to give you an idea, or my opinion, as to what has happened in the insurance industry and there are possible solutions that I see that I will get into but first of all I want to tell you the good thing that has come out of this. The very good thing is that for the first time in 45 years, since this industry was born, post World War II, it is now acknowledged as a business and these businessowners, for the first time, are going to come out of this with professional product that are offered to them as businesses.

They are no longer going to be referred to as "babysitters" because they are not. I have not seen one sit on a baby yet. I stole that phrase.

The good thing is that we have realized that we have over 1,200,000 professional providers in America. And in California there are 38,000 licensed and 32,000 active.

These professional providers had legislation moving to require them to have liability insurance in the fall of 1984. At the same time, in the fall of 1984, in October, to be exact, the insurance companies had a very short rope put around their necks and yanked very tightly.

They had been wanting your insurance dollars so badly that where they should have been charging you $5 for an exposure, they were charging 50 cents. They kept cutting rates, which has already been alluded to, to obtain the control of your dollar.

They were making more money on the investment of your dollar than they were on the insurance underwriting risks part.

They mismanaged their companies so badly and let them not get out of that, nobody has really told these big giants out there that, "hey you are a part of this problem and you have to be a part of the solution." You have been mismanaging your money so badly, our money, that you lost your reinsurance market in October 1984, 75 percent of the insurance companies, writing 95 percent of the insurance liability risks in America lost their reinsurance markets overnight. Just like that.

Now we have to picture the person who is going to solve this problem. The man who was in charge—I say man because I do not know of any women executive underwriting vice presidents at this time in the big companies sitting back in Connecticut—here comes Connecticut again, but I want you to picture this person making the decision.

I come from inside a company so I kind of understand what they did. The man is 63 years old and is about to retire. His wife never worked. He is in charge of all the underwriting profit or loss in America for his company.

He gets up in the morning at 6, he turns on the news and he sees the McMartin day care center losses. The defense costs are horrendous in that loss. There are no losses paid, just the defense costs.

He goes off to his office and is told how much money they are losing. He is told that he has lost his reinsurance markets. He is told he has to cancel half of his agency force. He is told that the other half can only write half the number of cases that they had the year before at triple times the premium and then he goes home at night and at 6 he sees the McMartin day school problem again and all he sees is this day care problem.

He is completely unaware of what a professional provider is or how important the professional provider is to the American work force.

He does not realize that if that provider does not go to work the next day, over 50 percent of his insurance-related employees will not go to work because they will not have a place to put the children.

That will have a ripple effect in the Federal Government. How many of your people use providers? In the State government and in my business I have 18 employees, 11 of which are dependent on providers during the day.

My mother got me involved in this in the fall of 1984 because she is the longest licensed day care mother in California. She has been at this for over 40 years so I have a personal interest in this also.

This 63-year-old man has never used a day care provider because his wife never worked. He is too far removed from his grandchildren, who are the children of the yuppies that are out now. Many of which I see in this room. He does not realize that his daughter-in-law and his son go to work everyday and they put their children in a provider's home. Now the provider's home is usually a little more expensive than a day care center. It does not get the Federal funding that the day care centers get.

So you see a different segment and a different complexion taking place in the provider home of 1 to 12 children. It is an entirely different complexion that it was post World War II.

The solution can be one of three. First of all, we can mandate, like our fine Senator from California has drawn a bill which is being announced this morning in California, Senator Seymore, mandating that insurance companies who sell liability insurance in a certain State, particularly California, has to assume on an assigned risk basis a portion of that liability.

I do not think when you force anyone to do anything that is a reasonable or successful solution. I have been working for 8 months with many, many insurance carriers. Over 500 to be exact. We have good records on that.

We now, today, and I have been—my agency is representing Scottsdale insurance in Scottsdale, AZ. We have just been approved in 12 States. So we have the day care insurance available in 12 States and we also have never lost the market for the centers and I want to stress that.

The rates are not nice but they are there. Mandating is not going to work in the seven major insurance carriers, of which most of them are in Hartford, CT, have now opened their doors to us and are sitting down with us and we are talking. We are educating the

63-year-old man that he has an underwritable risk which you have already alluded to and I appreciate that.

They have watchdogs take this business we are talking about, first of all they cannot be in business legally without a license. I would like for you folks to see what these providers go through to obtain a license.

It is not an easy licence to obtain. Secondly, they have a network throughout the United States like none you have ever witnessed. Good or bad news travels through this network like wildfire. You can announce something in California at 9 a.m. and by 1 p.m., California time, it has been heard if it is really hot news, by most of the providers. They have an incredible network. They are watchdogs. They are proud of their industry. These are proud providers, they are proud of their business.

I just want to give a little side-line. I have not been speaking out of 38 associations in California, I have spoken to 30 and what I found in each meeting, there was a growing force of husbands being involved in the family business and this is becoming a true family business with them. They come to the meetings and work with the wives and that way do not have to pay an employee to work to have 12 children. They take their business very seriously. I have been to some of their conventions, I have been to some of their training meetings and I will tell you this profession is a proud profession and moving faster than anybody, especially me, could imagine when I got involved.

This underwriting vice president has got to see that he has a risk that is underwritable and profitable. We talk about profit and I hear the losses. Mr. Coats explained the premiums versus the losses by St. Paul.

I have a statement on that Mr. Coats. They did not tell you that those losses were not from day care. Those losses are just like all the other losses that the insurance industry is throwing out to get out of facing their responsibility in this crisis.

They have never segregated the difference between a child care provider, a convalescent home, an elderly home provider and nursing homes. That is a fact. And the insurance industry is using their other losses to get out of facing this high profile risk.

That has got to be brought out. The insurance industry, if they understand they have an underwritable risk and the provider understands running a business and doing business is paying a reasonable premium for their exposure and their liability and these people can get together around a table and we can come up with products, which if you want me to go into detail, we have a theory that will work and I have discussed it with some of the major carriers and they are interested in your response. They are willing to set down with us——

Chairman MILLER. I hate to do this to a witness but I have just been informed that we will be scheduled for a vote shortly. If I can just ask you to summarize, so I can be sure we will have an opportunity to ask you questions.

Ms. YOCUM. OK, I will summarize very quickly. The solution that I think will work, we can continue on the route that we are going right now and educate, over a 3-year year period, enough insurance companies to get competition back in the field and that would take 3 years.

The other alternative is to turn to you folks in this committee and say you can solve this within 30 days if you will make a loan to an entity that is formed that will go to the carriers and let them bid for this money to give them their reserves that they do not have now and these reserves would be only for the day care providers or for the child care industry.

These reserves now relieve their problem. These reserves now allow us to immediately put into competition and put a quality product nationwide available at around a $500 premium per home. The $100 a year permium is gone forever. This would get this going. We have the right people lined up and ready to monitor it. The companies that would be awarded the contract would be based on competition and in 5 years that $10 million less than $100 per provider of the 1,200,000 providers in America, less than $100 for those people for a loan—a loan cost loan—would be repaid within 5 years to the Government to put back to work for another industry.

This product would be available for agents to sell throughout the United States so you are not taking away from private enterprise insurance.

This product would eliminate Federal funding. It is a Federal loan to solve a very sincere crisis that we are facing now. This is not giving money away. This is solving the problem—loaning to the insurance carrier who obtained the contract—or carriers, I think it should be 3 to 5—we have more details on this if you would like the summary in writing on it. But that I think that is the possible solution that should be researched.

[Prepared statement of Georgia Yocum follows:]

PREPARED STATEMENT OF GEORGIA YOCUM

First let me define who we are taking about. We are not talking about Day Care Centers, we are not talking about Pre-Schools, we are not talking about babysitters. We are talking about licensed in-home child care providers. There is a growing faction of men and women in this business, together these men and women are active in their associations and committees and are growing in numbers. The number of children that they supply provisions to, take care of and educate are anywhere from 1 to 12 children. This business has been growing steadily over the past 40 years and has evolved from a babysitting "Post World War II" term to a "now" profession that has not been recognized until the crises we are facing today. That crises being that these professionals can not obtain the same quality of insurance that Main Street America can.

Now that we've identified who we are talking about let's identify when the crises started. In October 1984, approximately 75% of the insurance companies writing 95 percent of the insurance liability lost their re-insurance market. How did this happen? For 5 years these insurance companies wanted your insurance dollars so badly that they continued to lower their premiums to obtain control of your insurance. Eventually the claims dictated that the premiums should have been higher. At the same time their investments turned sour, interest rates went down, the losses started climbing and chewing up their insurance dollar. The insurance companies that carried this re-insurance came in and said, "wait a minute, you have been running your business badly. You are losing money, you've put us in a bad position, and we're pulling our re-insurance." The insurance companies lost their re-insurance market and a very short-quick yank on the rope brought a halt to selling insurance in America at the rate and at the volume that it had been sold before. Exactly at the same time the legislators are mandating through different bills the requirement for liability insurance to these professional parents. That's a good bill, they should carry liability insurance if they are a professional business. But it was given to the parents in the wrong manner, and there is really nothing we can do about that now. So that you understand the repercussions of how it was presented, January 1, 1985 the bill was mandated in California, and I'm not sure of the effective dates for the other states, but when the providers and parents called to find out how to buy this insurance (they had never shopped for commercial insurance before) they were told by the top of the licensing bureaus, and at the legislative levels by their representatives, just pick up the phone and call your local insurance agent that handles your homeowners and auto insurance. We all know what happened then. They caused a mass of cancellations of homeowners and auto insurance because the people writing the nomeowners were not in the commercial underwriting business. They could see themselves defending the McMartin type case all over again so they got off the risk. In order for these providers to maintain their homeowners and automobile insurance they are now withholding the in-home day care information. Now not only can they not buy the commercial insurance, we've caused the mass cancellation of personal insurance. What are we going to do about it. Mandating it is not the way to make it happen. You know and I know that it may be one of the solutions in a lot of ways but the best thing for America today in this crises is to get the providing insurance carriers to understand that they have an underwritable risk. That's an educational process. And we need to get the providers that have to buy the insurance to understand that there is no such thing as a $100 a year premium any longer and to understand why the insurance carriers are frightened of their risk. It is not because they have lost money on them before but because they have a problem completely unrelated to the day care situation. We can solve it if we can educate the two factions. The cost of doing business in your home is buying commercial insurance, and it's going to cost $500 to $1000 a year.

We need to educate the decision makers at Hartford, Aetna, CIGNA, Fireman's Fund, and all the other insurance companies. We have vice-presidents in charge of underwriting throughout the United States who see the McMartin type cases on the 6:00 news and directly relate that to all day care. We can still obtain insurance for child care centers, higher rates, but we can get it. The education process needed here is this 63 year old man, who is the decisionmaking underwriter, about to retire, his wife never worked his children were never required to go to a professional provider. He doesn't realize that he has an underwritable risk. If we don't inform him that he does when he has a $1 to spend in the insurance market is he going to put that $1 risk in Main Street America where he has a lot of experience, or is he going to put it in the high profile of the McMartin type cases.

That's all he sees. He does not see these 1,200,000+ professional parents in America that if they don't go to work tomorrow the State and the Federal Governments don't go to work tomorrow, and my little tiny business with 18 employees doesn't go to work tomorrow. That's how important they are in the survival of America. In the business world they are vital. So we have to solve this problem quickly, efficiently and satisfactorily to both parties. Both to the 63 year old underwriter who can't relate to the fact that these "what he thought of as babysitters" are professionals who belong to associations who many have college degrees, and I have talked to many of them with masters degrees in education and varying areas who have chosen to stay home and raise 5 or 6 or 12 children. We have to educate him that when they got their license they went through a tremendous research. Their homes are inspected, their yards are inspected and they finally get a license. Now they belong to an association, if you think you've ever seen a network of associations you've never seen anything like the network of those licensed day care providers. Word travels good or bad with them, like wildfire, faster than you can telephone across the United States they've got it to a million providers. The network of association people are the best watchdogs we have. They care about their children, if they have a bad egg in their midst they aren't like some professionals who hide their head under their wing for their own reasons, they let other providers know. Their association is notified and they act swiftly to correct the wrong. That's the best watchdog we could ask for.

We've got rigid licensing, association membership, and if the insurance companies inspect all other commercial businesses why wouldn't they expend the same dollar to inspect a $600 to $700 or a $1000 premium for liability insurance. They can hire their own third party inspection drawn up to their own specifications and cut loose the $15 or $20 out of their premium to satisfy themselves that it is a secure risk. These are three very good watchdogs and the fourth if this is drawn properly, will be your local insurance agent who's the field underwriter who select these people. We will have a program that licensed agents throughout the United States can sell. That is the ultimate solution. We need five or six of the big carriers to sit down around a table and design the plan needs. We put in the exclusions that we need and if we need to legislate a cap on settlements, legislate a cap on settlements. Now we have created a solution to a problem that's profitable for all sides. The insurance carriers are going to share the risk, share the profits and share the losses. The providers are going to have a product that they can afford and should the losses be good, should their watchdogging be as effective as we anticipate it to be, there are good profits. They are going to share in that profit. Now we can lower the premium for them in lieu of dividends or this type of thing.

There are other avenues they can go such as self-insured. You and I both know that won't work at this stage in the game. It may be in the future 5 or 6 years from now. But at this time let's help them to not be premature. The other solution is that we have a Federal Government program or a guaranteed insurance program and that is federally subsidized and takes out of the realm of reality and keeps us away from having free private enterprise. Let's solve this with the parties involved understanding each other's problems and accepting the solution that can be gathered from these types of meetings. We are very close, at least the insurance companies are not shutting their doors any longer, they are opening their doors and saying listen let's sit down and talk. We're that close to having a solution. So if the Federal Government today wants to do something I challenge you to get together and have a meeting and share what we are willing to do to get this going in the right direction. We've already started, we are here together today, we have some markets available, 3 months ago we didn't. A week ago we only had one market, now we have two in California. We need to keep competition in this to keep things healthy.

Chairman MILLER. Thank you. Congressman Rowland?

Dr. ROWLAND. Thank you very much Mr. Chairman. I just wish to complement you and Mr. Coats, the ranking minority member on this subcommittee—this committee—for focusing on this area. I think it is an excellent hearing and certainly there has been mentioned relationships between what we are talking about here and other areas.

I assume, Mr. Chastain, that you were talking about being called Daniel of the story of Daniel in the lion's den, is that correct?

Mr. CHASTAIN. Yes; I was.

Dr. ROWLAND. Well, as I recall that story, when Darius threw Daniel in the lion's den and went back the next morning, he found Daniel to be all right, of course, this was because the lions' mouths had been sealed. Those who were responsible for Daniel being thrown in the lions' den were themselves thrown in and they were torn asunder. So, I think you are going to be all right.

Maybe we can find those who are causing the problem and tear into them. What I wanted to mention was that there seems to be some common thread here. I want to ask about some of the areas that have already been mentioned for example, the problem with professional liability insurance where we have seen the cost of premiums just escalate out of sight.

Even those medical organizations that have formed their own mutual insurance companies are now finding that they are in trouble also, because of the increasing number of lawsuits and the threat that hangs there.

Someone mentioned earlier the fear about what will happen. The people that are running the day care centers now find trouble getting liability insurance. While they have not had any suits to happen that much, they are still very fearful of what may happen.

I was at home this past weekend and was talking with someone there who manufacturers heavy equipment in the forestry industry. He tells me that he is not going to be able to get product liability insurance any more after this year.

It was mentioned earlier about not being able to get contractors to clean up hazardous waste dumps because they cannot get insurance to cover them in case the dump is not clean—we could just go on and on.

It seems to me that there is a tremendous black cloud hanging out here pulsating that is just waiting to explode. My question to you is this, Is there some common thread here, might it be the fear of suits that might take place? How can we deal with that, should we look at the possibility of changing our tort system in some way?

I do not know. I am just looking for answers because it affects these people who run these child day care centers just as it does many areas in our society. Do you have any thoughts on that, without taking up very much time, but just a comment or two?

Mr. **Silverman**. The fear is very real. The adverse publicity, historically, has brought about more claims. We see a direct correlation of the number of claims activity, whether they are founded or not is academic.

The fact is that the claims activity is there because of the publicity and the cost of litigation for defending these allegations are very expensive and that is one of the reasons why the insurance companies are a little bit worrisome about what they might be getting into.

Dr. **Rowland**. I see.

Ms. **Yocum**. I think to put a cap on the losses would be something that could be looked at. I know there are a lot of legal ramifications on that but if you put a cap on an award, then what you are going to do is see a lot of the deep-pocket insurance attorneys stop taking these cases because they can get $2, $3, $4 million if they could only get $300,000 per loss, a lot of them would disappear very quickly and the suits would be settled reasonably quickly.

Dr. **Rowland**. Do you think that could be addressed on the Federal level—I know that there are some States that have enacted legislation to put a cap on the awards and it has now been overturned by some of the State courts in the area of professional liability. Do you think that should be addressed on a Federal level?

Ms. **Yocum**. I think it should be addressed on a Federal level because this is a Federal crisis and I think it should be reacted on very very quickly or we are not going to get insurance companies back in the marketplace like they are tiptoeing into now.

Dr. **Rowland**. Mr. Chastain, do you——

Mr. **Chastain**. I would not approve of a cap at this time. I think that we should take the legal system as we have it and find a way to pay for it.

Dr. **Rowland**. Do you think there should be any consideration given to addressing our tort system on a Federal level?

Mr. **Chastain**. Yes; I think there should be.

Mr. **Silverman**. This is not the first time that the subject of tort reform has been brought up, I am sure. My only comment, Mr. Rowland, about a cap is that I do not feel qualified to establish a cap on a claim of an 11-year-old child involved in an accident—this is a claim that we have now—who is literally a vegetable. I do not know how you could put a cap on that type of a claim so depending on the circumstances of the merits of a claim, I think each claim has to stand on its own.

Dr. **Rowland**. Mr. Chairman I could pursue this for another hour or two but I will terminate it right here and yield back the balance of my time.

Chairman **Miller**. Thank you. Congressman Coats?

Mr. **Coats**. Mr. Silverman, you said that child care was an insurable risk at an affordable cost. I assume in that statement, by that, you meant that there would have to be certain exceptions and limitations. Perhaps, you just said that we should not have a cap, but if child care is an affordable risk—an insurable risk at an affordable cost, what kinds of exceptions would we be talking about in the policy? What kind of items should we be exploring? What questions should we be asking the insurance companies in terms of what would the policy look like? What would the exceptions be and so forth?

Mr. **Silverman**. Well, with a little bit or pride of authorship, our particular insurance policy is a specially design, what we call manuscripted form. To my knowledge, it is the only one in the country that addresses day care by definition. There is no problem with the insurance form itself.

Insurance companies, for years, have excluded, either directly in the policy, or by inference, criminal acts and that goes on to sexual abuse and criminal abuse. The costs of defense by the policy is necessary. Our policy happens to exclude any loss arising out of sexual abuse but we will defend for the allegations of that sexual abuse.

There are a lot of cases that are brought about without merit and the providers are innocent. When I say that the risk is insurable at an affordable cost, I only ask that the insurance companies evaluate the risk as an actuarial exposure, not from an emotional standpoint.

I would like them to turn off their radios and not read their newspapers for about 60 days and look at some of the statistics that we have available for them and if we can get pass that emotional impact, we can demonstrate that the cost can be affordable and the risk is insurable.

Mr. **Coats**. But part of that problem would be what you characterized as late reporting or long-term risk. You cannot necessarily put an actuarial table to (particularly, in a situation where you have a minor that is able, 10 years later, once he becomes majority age, to file suit) an alleged abuse or neglect or negligence that might have taken place 10 years prior when he was 8, 10, or 12 years old. You cannot really put an actuarial table to that at this point can you? Is that part of the problem?

Is that part of the emotional response that you are getting from the reinsurers?

Mr. **Silverman**. In our opinion, and I think we can substantiate that with the underwriters, that a change in the way they evaluate their losses and the way they are carried forward in the rate makeup has to be made.

Currently an insurance company will allocate the losses that it receives in a given year with known reserves against the currently collected premium.

All too often the insurance companies, who are in the business of spread-of-risk, lose sight of the fact that they are not doing that.

We have insurance companies that have reported $1 million losses on $300,000 in premium.

What we ask is, "what are the losses on that specific class of business on a national scope?" I have publicly made the statement that, "if care providers are not insurable because of this terrible publicity that has been going on, then I submit to you, neither are homeowners, aircraft companies and a number of other institutions that are insured throughout the United States."

We had two bombings of an aircraft in the last 60 days. I do not see insurance companies canceling all the aircraft industry. Maybe it is because the premiums are a little different.

Maybe it is because they have better statistics. In California, we recently had 39 homes destroyed by arson and 11 people killed. I do not see a mass of insurance companies canceling homeowners insurance policies nationwide. I have yet to understand why, other than the emotional impact, are they canceling the day care providers.

Mr. Coats. But that potential long-term exposure could be—I do not know if I want to use the word—"valid reason," but could be a reason. It is the potential exposure to the risk. When they had the oil crisis, when they were bombing the oil tankers in the Middle East, insurance rates either doubled, tripled, quadrupled or insurance was not available for a period of time because that perceived risk was there.

It was not necessarily based on actual experience but it was based on what might happen. Insurers decided—Lloyds of London decided that it was too big a risk to carry at that particular time. So that is always going to be a factor.

I guess my questions are: Are there things that we can write into the policy? Are there agreements that we can make when we sit down with the care providers and insurers around a table? Are there elements that we should be looking at that would quantify potential risk and, therefore, bring insurance back into the business?

Mr. Silverman. The tail, as alluded to earlier, is a major concern of the insurance industry. It is being addressed currently by the industry on liability exposures across the board. There is work being done now by the industry for a form change that will help eliminate the problems of the tail and direct the cost for that tail coverage to those industries that have the need for it.

Part of that stems from the tort reform that we were talking about earlier and I am not prepared to go into that at this time because that is another hearing by itself.

One of the things that is going to have to be done is the cost of the insurance is going to have to keep pace with the losses and with the tail.

What has been the problem for the last 12 years is from 1977 through 1983 there was not a rate increase and yet the tail losses were mounting and no adjustments were being made in the premium to cover it.

What they were looking at was a long period of low premiums to cover an equal period of higher losses that were developing in later years.

Mr. Coats. So the bottom line is that you think insurance can be written, but the cost to the day care providers is going to be higher and the limits of coverage are going to be, perhaps, more narrowly defined and the deductibility is going to be higher. In other words, it is going to cost more to get insurance, but it can be provided. Is that your bottom line?

Mr. Silverman. Yes and I think so at affordable rates, even if it means some sort of government subsidy for the lower income people and the deductibility of care provider-cost to the consumer.

Chairman Miller. Congressman Monson?

Mr. Monson. Thank you, Mr. Chairman. Ms. Yocum, how does an insurance company build adequate reserves on borrowed money?

Ms. Yocum. It would not go to the insurance company. It would go to a policy that would be insured by an insurance company and those reserves—right now the companies do not have their reserves. That is their biggest problem.

Where they had, let us say, $1 million a year ago, they may have only $100,000 they can put out at new risk today. When they make that decision, are they going put that money that they have now—$100,000 that they can put out to risk because for every dollar they take from you they have to put some money in reserve—are they going to give it to main street America where they have a lot of experience and their chances of a slip and fall are a lot different than this risk or are they going to give it to the day care that is such a high profile.

Not necessarily a high risk, but a high profile business now. You do not give it to the company, you give it to a policy reserve. So if you have a policy reserve that is, for lack of any other name, a provider's insurance group policy, that these providers can join and pay their premium to—if you want to see the acturarial formula, it will work because there is enough money provided that can be collected on a premium basis.

The problem here is getting—finding that insurance group or carrier, because it is going to take a group, if they do it on their own, finding that carrier or a group of insurance carriers that have the money they can actually set in reserve, and they do not have it.

Why they do not have it is not the problem. That is not going to help the solution. They do not have it. So I say if we can come up with a reserve and we walk into a carrier and say, "OK, this is our own reserve for own group policy. We want to buy your paper." We now have created something almost instantaneously and then you have the premiums coming in and you have your own reserves building and then you will be able to pay that money back to the government that created the reserve. That is all you need.

Mr. Monson Well, that is quite a bit different than the way it came across in your original testimony. I appreciate that explanation, but I would like to see more detail on it so I can try to understand it a little better before I sign off on that.

Ms. Yocum. It has been done successfully. I can show you the track record so the wheel has been created. Not in day care but in other forms.

Mr. Monson. Well, if you could get me some information, I would certainly appreciate it.

Ms. Yocum. I would be happy to.

Mr. Monson. Professor Chastain, as far as insurance companies are concerned, are they required to do anything with reserves that they may have in areas that they decide to no longer insure, or are they free to just keep those reserves and apply them to other areas of insurance?

Mr. Chastain. Well, those reserves are there in order to cover the losses that have occurred on whatever policies they were writing previously. They have to maintain those reserves to let that old business run off, but, if there is money left over after the business runs off, then they get to keep it.

On the other hand, if there is a shortage after that business runs off, then they have to make up those reserves from other places.

Mr. Monson. Is there any evidence that they may have accumulated reserves in excess of what they will be required to pay out?

Mr. Chastain. Probably to the contrary. In most of the other areas that involve long tails, companies have had to go back and supplement their reserves.

Mr. Monson. What do they have to do with the regulators before they can discontinue providing insurance, anything? Or, are they free to do it any time they choose?

Mr. Chastain. It differs from one line to another and how much they want to discontinue; but if they want to discontinue writing a whole State and withdraw from that State everything they do, then they would have a right to do that.

Otherwise, the State insurance commissioner has some areas of moral suasion and, sometimes, law to protect them.

Chairman Miller. It is either on or off.

Mr. Monson. Do we have a situation with the companies? Or are all liability coverages covered in the same reserves or do they segregate them according to different lines, such as automobile, day care providers, et cetera?

Mr. Chastain. There are several different ways the companies have of reserving; but, in some cases, they have individual policy reserves where they know that the reserves are for individual losses that they have.

And, in other cases, they have class reserves that cover a whole line of business; but, in any case, they would doubtless be able to separate child care centers from their other lines of business internally.

It would be a matter of getting that kind of information from them.

Mr. Monson. And does that vary according to State, also, in the State insurance department requirements?

Mr. Chastain. Probably not. Companies could—it is my impression that the accounting in this place is uniform.

Mr. Monson. Thank you very much.

Chairman Miller. Congressman Smith?

Mr. Smith. Are we not really dealing with something that goes beyond your industry and beyond the providers here into a more far-reaching societal problem? Are we not all essentially—depending on which side of the fence we are on—if we are the suer we want to get as much as we can get; if we are the suee, we do not want to lose.

I do not know if those words are correct but the idea is. I think that the discussion of some type of cap or scale or some sliding scale or something seems to me to make sense; and I think we probably should be looking along those lines.

I do not think we can continue to have unlimited liability for everything that happens. Somebody could fall coming in here, and what is a broken leg worth? Is it worth $4 or $5 million? Is it worth $4,000 or 5,000?

Until we determine that as a society, either through the laws or some other way, I do not think we are ever going to solve this thing. Essentially, an insurance is not going to insure if they do not know what the parameters are.

You cannot blame them for that. They are a business. On the other hand, you certainly have to realize—somebody, I think Mr. Rowland mentioned—I was at a testimony last Monday on toxic waste and it was the same thing.

The companies involved with toxic waste cannot get insurance either. It is the same thing. It is a societal thing, I think, that goes beyond this. I would just like to conclude with one question or comment. At least two of you, regarding insurance, testified that you felt that it should be—I believe you said it should be—affordable and available for day care providers. So, I would suggest that the two of you that said that get together with the folks that are going to be cut-off from their insurance before you leave the room and give them some short-term help while we try to deal with the long-term problem. Thank you.

Chairman MILLER. Mr. Chastain, you indicated you thought the insurance providers may be sorting out the risks for child care. Yet the first panel and Mr. Silverman seemed to indicate that the withdrawal from this field is based more on a sense of panic.

It seems more like a general retreat than a sorting out of the risks. Do you have any statistical evidence or any evidence from the insurance companies that suggest that there is a careful sorting out of benefits and risks?

Mr. CHASTAIN. No, we have heard some comments about that. Someone commented that Aetna is still in the business, and we have heard from both the other two speakers that they have a market. I think that would be a question worth checking into. To see whether the testimony we got today from some people is universal or whether there are markets. I do not know the answer to that question.

Chairman MILLER. My understanding, from watching TV ads, is that when an insurance company finds that one of their insured is in trouble, an agent comes in and says, "you better put a rubber stopper on that door so somebody does not hit their head and you better guard that machine and you better make these improvements and we will continue to underwrite you and that will lead to fewer losses being incurred," and that it is in the interest of the insured and the insurer to go through this process.

What we have here is a notice of cancellation—of immediate cancellation.

Now maybe there was a sorting out what went on for the past year and this decision was made in a very rational yet undisclosed fashion. But for the moment we do not have any differentiation being made between licensed, unlicensed, family day care, center day care, YMCA-provided day care, church day care, private or nonprofit, government run—we do not seem to have any of those kinds of processes you would think somebody would go through before they decided a risk was assumable or not assumable.

It appears that an entire class has simply been thrown out and the only question asked was, When was the policy up for renewal?

You seem to back that up, Mr. Silverman. That from your experience in providing substantial coverage to a large number of people in child care, this a wholesale retreat, rather than a careful sorting out of assumable risks.

Mr. SILVERMAN. The definitions——

Chairman MILLER. You do not have to accept my conclusions, but this discussion has left me a little bewildered. To suggest that there is an insurance cycle that the industry goes through is one thing, but to suggest that results in a careful sorting out is misleading. It is more like an undifferential reaction.

Mr. SILVERMAN. I think that you can draw a fair conclusion from that, yes.

Chairman MILLER. Well, it is a disturbing situation.

Mr. CHASTAIN. I understand that Mr. Miller and I understand the frustration.

Chairman MILLER. Congressman Smith?

Mr. SMITH. Just one quick follow-up question for the providers. In your conversations with the insurance companies, did they give you any hope, for example, if you were to offer some way of tightening up your interview process—I assume they are afraid of child abusers and that sort of things, but were there any parameters given there, that if you give us a background investigation on all of your people, this sort of thing? Just for curiosity.

Ms. CHESSNOE. Day care providers have been encouraged to join up with an association and we feel that by saying that, they are saying that an association would provide them with certain benefits. They are looking at the association, for example, as a network which would give support to the various providers in various areas. That is, support and just coping with their job is one and by relating to others, be able to do a better job.

We also have meeting in which various issues that have to do with day care are addressed and these would be concern with various problems so this is of benefit.

We also encourage the providers to attend other various kinds of meetings with the understanding that these have as a basis, education, you see and further education of these people. In other words, these associations are promoting professionalism.

Ms. YOCUM. Mr. Smith, may I just say something? I do not think we have gotten across to the insurance companies even if they wanted to give us product in January, could not. They did not have the reserves and they did not have any reinsurance companies.

They could not, even if they wanted to. That is something real important for you to understand problem. They just do not have the reserves and what little they have, they have chosen to put in safer places.

Chairman MILLER. Let me beg to differ in part with that conclusion, because we have seen in a limited fashion with NAEYC that the industry suggested that for an association that had some standards they could write at least partial coverage. That does not suggest there is a wholesale solution to the problem. But somebody had some reserves to extend some coverage in some instances.

Ms. YOCUM. They did want to improve their risks on that but that was an isolated case. The 1 to 12 children in a home, there is absolutely nobody. Nationwide owned Scottsdale insurance and happened to have $1 billion.

They gave Scottsdale $1 billion. That is the only insurance company in America without a capacity problem that will underwrite this risk today.

Mr. SMITH. We have heard testimony that there have not been huge settlements in this area so why would they not have reserves?

Ms. YOCUM. You are right. It is because, I think we have to help you understand, their reserves on their entire block of insurance business is one word. When I referred to setting up our own reserves, if we come to you with a group policy and we have our own reserve, you cannot use our reserve for someone else. We own that.

We own that reserve so if I transfer my group from Aetna to Hartford and Hartford accepts my risk, they accept my reserve on my group policy. They cannot use that for automobile dealers. They have to use it—it belongs to my policy number——

Mr. SMITH. Where is the money? The settlements have been minimal by testimony previously, and you have been insuring so where are your reserves?

Ms. YOCUM. OK, they have been insuring these people on a loss basis, not a group basis. There is a big difference in a group policy that you own and we will call that a retention factor, so that the providers that pay the premium would also share in the profits with the insurance company and I—the way you set up a policy and it is different than a general underwriting of insurance.

Mr. SILVERMAN. I think that one of things that we are confusing is the word, reserves with surplus. Reserves are set aside by insurance companies to pay claims. Surplus is what they use to write the insurance business with.

Unfortunately, I have to disagree with my distinguished colleague over here. I think that the surplus capacity is there for single insurance companies or many insurance companies to write the risk at hand.

Mr. CHASTAIN. I agree with that. The figures that you have there show, for example, by this surplus, the surplus figures have been going down over the last few years. In 1983 they were down to 1.66 to 1 and in the industry it is generally considered safe to be writing two to one or even three to one so there is excess capacity, generally, in the business.

Mr. COATS. Well, there is always capacity at a certain premium I would assume. The question is more, "Why are they bailing out of the business altogether?" Either they feel day care providers cannot pay the freight on the kind of premium they feel they would need to provide, or they just fear that something is boiling out there. They are not sure what; and, all of a sudden, there are going to be lawsuits all over the country. The McMartin case is the tip of the iceberg. All of a sudden, we are going to be flooded with liability claims on problems in day care centers.

I guess the conclusion is that we have to get the insurance companies up here to tell us why they are making the decisions they are making and what is motivating them to do so.

Mr. **Chastain.** I would like to make one other observation if I may. The people who would like to see the situation stay the same—not to have any more premiums and to continue to have their coverage—it seems to me are assuming one of two things. Either the insurance companies that feel this is bad business are incorrect. They are over-reserving, and the time is going to prove that they do not need that much money. This happened in the medical malpractice business. The doctors went out and set up their own companies, and now they are finding that maybe there was something to the long tail after all because the companies that were set up were in trouble. I would want to check carefully to see whether the insurance companies were correct in assuming that the reserves they are setting up are accurate. If you assume that they are accurate in the rate, and you still want to maintain the rate at the same level, then what these people are saying is what they want a subsidy from somewhere.

The subsidy can come from a lot of different places. It can come from the other policy holders or it can come from the stockholders or it can come, as has been suggested here, by direct Government infusion of funds. It can come from some place.

I am not at all against a little Karen going to day care school. I think she should. The problem is that insurance companies are a bad way to provide a subsidy, to shift income from one group to another. There are a lot more efficient ways to do that than attempting to shift income through the insurance mechanism.

Chairman **Miller.** I think Congressman Coats is saying what may be the second question. The first question is why the withdrawal from the field.

There is an assumption that the marketplace would provide this coverage at a certain premium. The question then may be whether or not people can afford that, and you may have to deal with that issue. But that is not what a lot of these providers are being told. They are told that coverage is not available at any premium.

That is a different issue. We have to cover that one first. Then the question of what the market rate is, and whether it is affordable may have to be attended to. But the first question is the more troublesome one. How was the decision arrived at to discontinue the coverage on a wholesale and nationwide basis?

Well thank you very much for your time, testimony, and expertise. Thank you to the members of the committeee for participating in this morning's hearing.

It is the expectation of the chairman of the committee, and I think the members of the committee, that we will have an opportunity to have the insurance industry come before the committee and help us to resolve this issue. Thank you.

[Whereupon, at 12:30 p.m., the hearing was adjourned.]

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CHILD CARE: THE EMERGING INSURANCE CRISIS

TUESDAY, JULY 30, 1985

House of Representatives,
Select Committee on Children, Youth, and Families,
Washington, DC.

The select committee met, pursuant to notice, at 10:15 a.m., in room 2212, Rayburn House Office Building, Hon. George Miller (chairman) presiding.

Members present: Representatives Miller, Lehman, Monson, Coats, Johnson, Sikorski, Boggs, Rowland, Wolf, Weiss, Wheat, and Boxer.

Staff present: Ann Rosewater, deputy staff director; Jill Kagan, professional staff; Carol Statuto, minority professional staff; Maureen Mingey, minority staff assistant; and Joan Godley, committee clerk.

Chairman Miller. The select committee will come to order for purposes of continuing our hearings on day care liability insurance and the problems presented to the child care industry and to those of us in policymaking positions by the withdrawal and termination of these policies.

At this time, I'd like to recognize Congressman Coats for any statement that he may have.

Mr. Coats. Thank you, Mr. Chairman. I'm pleased that we could have this followup hearing to our earlier hearing, at which we heard some disturbing testimony. The bottom line was that the day care centers are either having considerable difficulty or finding it an impossibility to obtain insurance coverage.

There were a lot of questions raised at that first hearing that were left unanswered. I think the purpose of the hearing today is to ascertain some of the answers to those questions. Do we, in fact, have a crisis? What is the extent of the crisis in terms of insurance for day care centers? Is it true, as some witnesses said, that no insurance is available at any cost; and, if that's the case, why is that the case?

What factors have contributed to the decisions made by insurance companies to not underwrite this form of risk? On the other hand, some indicated that, yes, insurance is available but that premiums have skyrocketed. If that is true, we need to ascertain the causes. Why have they skyrocketed? What has been the factual basis for the determination that premiums need to rise as they have? What is the perception in the insurance industry, what is the reality in the insurance industry of the risk of insuring child care?

These are all, and only some, of the questions that I think are begging for answers. We hope that the witnesses that are here before us today can supply this information, so that we can go forward and make a correct assessment of this situation.

So I commend you, Mr. Chairman, for moving so expeditiously on this subject, and I look forward to the testimony that we are about to receive.

Chairman MILLER. Thank you very much, and I want to thank you for your involvement and your support for these hearings. I think you are quite correct: we have got to determine, almost on an immediate basis, the extent of this crisis, which sections of the industry are being effected, and whether or not we can expect, as people have suggested, that this crisis will grow much greater as the school year begins in September.

And I think it's very important that we understand, again, the policy impact. If in fact it can be proven that it was a wise decision by the insurance industry to cancel or to raise the premiums, or not to provide renewal, we must then understand what that means for the child care industry. We cannot leave them in that breach. There must be a positive change, because providers cannot offer the kind of child care that all of us would want for our children in uninsured facilities and with people who do not carry liability insurance.

So, even if, and I'm a little skeptical that it can be proven at this time, even if this was a wise decision by the industry, it's an unacceptable result for this industry, and unfortunately those who would be required to respond are going to be government entities, either at the State level or at the Federal level.

So, let us proceed here.

Our first witness will be the Hon. Edward Muhl, who is the insurance commissioner for the State of Maryland, and he will be testifying on behalf of the National Association of Insurance Commissioners.

Mr. Muhl, welcome to the committee. I understand that you have some scheduling problems, and I apologize for the lateness of the starting time of this hearing. We had a Democratic caucus, and as I said to Congressman Coats, I'm now convinced that Will Rogers was right. I belong to no organized party, I'm a Democrat.

But we're sorting things out, slowly. But thank you very much for your willingness to testify.

[Opening statement of Chairman George Miller follows:]

OPENING STATEMENT OF HON. GEORGE MILLER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA, CHAIRMAN, SELECT COMMITTEE ON CHILDREN, YOUTH, AND FAMILIES, JULY 30, 1985

Today's hearing continues our investigation into the insurance problems of child care providers.

Two weeks ago, at our first hearing, child care providers and insurance agents provided a disturbing picture of the nature and extent of the problems they face.

With little or no advance warning, family day care homes and child care centers across the nation have experienced mid-term cancellations, nonrenewals, dramatic rate hikes, and severely restricted coverage.

Today, we will hear from representatives of the insurance industry. We are very interested in hearing their position, and reviewing their plans for providing coverage of child care programs in the future.

Our goal is to find a speedy resolution to this problem. Child care programs must be able to operate without interruption.

Loss of this essential service jeopardizes millions of American families in all our communities. This is a serious concern for members of Congress, as well as for policymakers at the state and local level.

Whatever factors may have led insurers to retreat from providing liability coverage, failure to provide adequate and affordable coverage for child care is untenable.

I look forward to the testimony we will receive today, and the opportunity to work closely with both the insurance industry and child care providers to develop a timely solution to this problem.

STATEMENT OF EDWARD J. MUHL, INSURANCE COMMISSIONER, STATE OF MARYLAND, ON BEHALF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Mr. MUHL. Thank you, Mr. Chairman. On behalf of the NAIC, who I represent as well, in addition to being the insurance commissioner for the State of Maryland, I very much appreciate the opportunity to appear before you and to offer some thoughts, concerns, and hopefully some directions.

I have submitted briefly some written testimony that hopefully you have before you. I'll just talk around that particular piece of testimony, and just give you an idea, if you will, where the day care industry is in relation to the whole of the business of insurance. There have been some massive problems, Mr. Chairman, for the insurance industry over the past couple of years.

They are pretty much at the end of a down cycle a cycle that has been a little more unusual than the norm of the cycles that have occurred in the past. It's rather severe. I know, since the beginning of the year, I have signed in Maryland, alone, 20 impaired or insolvency notices of insurance companies that no longer are allowed to write the business of insurance, and most of them have in fact gone out of the business of insurance, and been declared insolvent.

Now, there are a lot of reasons for this down cycle, but I suggest to you that the day care industry is sort of caught up in the total of this down cycle as are most of the commercial lines. So we have not only the day care folks, but we have long haul truckers, the nurse midwives, municipalities, counties, the list just goes on and on.

Now, with that, the insurance industry has in fact lost a tremendous amount of money. They have gained some through investment income but that's not true for all of the companies. A lot of individual companies have taken a severe beating. As a result of this, the capacity to insure has dwindled. Now, again, I suggest to you that this is individual companies that are making these decisions, and not the industry as a whole.

With the capacity crunch or, if you will, the shortfall capacity, which not only affects a lot of the American companies but has also branched out into the reinsurance facilities, such as Lloyds of London, and others, now with that, we understand there's going to be approximately a $67 billion shortfall in oapacity for the remainder of this year on into 1986.

That means that there's going to be about $67 billion worth of insurance not being sold for the remainder of this year into 1986, that was sold previously, in 1984 and previous years. Now, the companies are having to make decisions on an individual basis. Where to they place the remaining capacity. Do they put it in lines that are more at risk and with the uncertainty that's involved with the higher risk lines, or do they place it in the more traditional risk lines where they've been known to make a profit, particularly at less risk over the years.

And those decisions are being made to place it in less at risk lines, and the more traditional lines. Now, that has caused the crunch, if you will, or the capacity shortfall for a lot of the commercial lines of business. Now, with reference to the day care, I think, and very unfortunately so, that the day care industry has been deemed or termed by a lot of the individual insurance companies as being higher risk.

A lot of this has come as a result of a lot of the national publicity that has been associated with sexual abuse and child abuse. Unfortunately, as I say, the whole of that industry has been tarred with that wide brush, where in fact, it's only been a really small minority of the day care facilities that have participated in such abuse. The whole of the industry is being tarred with that brush.

I think the insurance industry is looking at this point and suggesting it's a matter of time before the hammer falls and the law suits come in with any degree of frequency for they are going to have to then expend a large amount of funds for defense of some of these day care facilities.

Now, as to the reality of the situation, the answer very simply is that we have not seen, through the NAIC, or myself, as an individual Commissioner, a large number, if any at all, of actual cases of child abuse where there was an actual action brought against the day care facility. I think it's more of an insurance hysteria than it is anything else, more or less, if you will, the industry anticipating that that's what's going to happen in the very near future.

So with the capacity crunch, the capacity shortfall, there is this thought of the industry to place their business in less at risk lines, and not to take the chance. And again, I suggest to you, there's going to be a tremendous amount of insurance not being sold this year. But I say, it's affecting not only the U.S. companies, but it's really international in scope. And it's not just Maryland or any of the individual States.

There are several things that the National Association of Insurance Commissioners have been doing, as well as the individual insurance commissioners. One of the things that we're trying to do is establish a dialog with the industry as a whole, with the several individual companies that are still writing this business, and those that have elected to get out of that line of business, to discuss with them, or to open this dialog suggesting to them that it's a good idea to really sit down and look at the actual realities and the facts of this.

Again, we're talking not an industrywide problem for the day care but we're talking about a minority of the day care facilities participating in abuse. If we can separate those issues—and I think we can—and suggest to the insurance industry that these people are insurable, there are other aspects of need for insurance that these people have, general liability aspects. I don't think any insurance company ought to pay for any facility that participates in abuse of the children.

So we're talking to the insurance industry about making various exclusions in their policy to exclude that aspect out of the policy, which I think would also increase the availability and not put the insurance companies, individually, at a tremendous exposure of risk, and accomplish the goal for everybody.

I had my staff, as late as of this morning, to review 28 companies that we have licensed in Maryland, who are in the business of selling insurance to the day care facilities, and I'll just give you these numbers as they were given to me this morning. There were 28 companies that were surveyed. Fifteen are no longer writing day care facilities. They have withdrawn totally from those lines of business.

Thirteen are continuing to write. Out of that 13—and I'm going to break this down—6 are renewing existing policies. They are only renewing, they are not taking on new business. Two of those companies are continuing to write group only.

Two other companies are continuing to write church affiliated day care facilities, only. And three companies are continuing to write with absolutely no restrictions. Now most, if not all, at this point have gone to an exclusion with reference to the sexual abuse or the child abuse situation and probably all of them will before much more time expires.

Now I suggest to you that there is a market. One of the things that we have done in Maryland, we we're going to convey this on, hopefully through the National Association of Insurance Commissioners for use through all the State jurisdictions, is a market assistance program, to attempt to match up the existing capacity with those companies that are out there still writing with those individuals or groups still in need of the insurance.

Now, we created this market assistance program in Maryland, and we were successful in obtaining the necessary insurance for the nurse midwives, some of the asbestos abatement contractors who could not get insurance, and we hope to expand this into all of the commercial lines to use our facilities, each of the State facilities, to find out where the capacity remains, and to help those people get insurance.

So there are a lot of efforts and I think we are successful, in most instances, in matching if you will the capacity with the individual that has the need or the group that has the need.

Now, one last thing, Mr. Chairman, if I may. There was one company, it was a California-based company, that wrote the bulk of our group day care facilities in Maryland, who was having some financial difficulties and at midterm, canceled the policies of 240, I think it was 242 of the group centers in Maryland.

I have recently issued an order after looking at the solvency aspects of the company issuing the order that this company has to remain on the policy and cannot midterm cancel nor can that company midterm policy increase or rate increase. So we, at least on a short-term basis, solved a great deal of the problems that we are facing in Maryland, and we are still seeking the longer term solutions and I think we can find that through the efforts of all the individual Insurance Commissioners and through NAIC.

Now, Mr. Chairman, you have, in your kind invitation for me to appear, submitted several questions. I'll be more than pleased to answer these individually, or hopefully I've just touched on a few of them, but if you have any other specific questions, I'll be more than pleased to offer any comment on them.

[Prepared statement of Edward Muhl follows:]

Prepared Statement of Edward J. Muhl, Commissioner of Insurance, for the State of Maryland

My name is Edward J. Muhl, Commissioner of Insurance for the State of Maryland. I am here representing the National Association of Insurance Commissioners as Chairman of the Commercial Lines—Property and Casualty Insurance (D) Committee.

On behalf of the NAIC, I extend our appreciation to the Chairman and members of the committee for extending an invitation for us to appear and offer comment concerning the availability of insurance for child care centers and others in the child care industry.

In order to more fully explain the difficulties now being experienced by the day care facilities, it would be appropriate, in my opinion, to brief you on the history and the problems that are being experienced by the insurance industry as a whole during this period of uncertainty and troubled times. I will also attempt to indicate the efforts that are being made by the various insurance commissioners as well as the National Association of Insurance Commissioners in seeking a resolution to the problems that face the day care industry.

The business of insurance has traditionally been cyclical which usually results in negative underwriting at the low end of any given cycle. The present cycle is much different than the norm and much more severe. What began as a traditional cycle in 1980 has turned into a disastrous five-year period due in part to the combining of several forces not necessarily present in previous cycles. One of the uniquenesses of this cycle is that it is international in scope and not just confined to the United States companies. The reinsurance market has been affected by the adverse loss experience and low premiums captured. This is the first time, to my knowledge, that the reinsurance facilities have sustained a continued loss as a whole.

The financial solvency of many of the United States companies is at question and, therefore, is being closely monitored by the National Association of Insurance Commissioners as well as by the individual state jurisdictions. There are many reasons for the financial crisis which I will note briefly for your information. Simply stated, there are several factors not within the control of the companies that range from high interest rates, excess capacity, to the status of world economies, to the entitlement attitude reflected through our tort system and so forth. There are several controlled factors, one of which, again simply stated, reflected an unprecedented industry wide participation in what is known as cashflow underwriting. Good sound traditional underwriting practices in properly pricing a particular risk were cast to the wind in order to capture market share. This, in turn, allowed the companies to invest the low premium dollars for high yields during this period of record high interest rates. The cycle is ending, interest rates are down, and the losses are mounting which, in turn, are exceeding the premium levels charged by many of the companies. Not all companies participated in such practices, but a fair majority did thus aiding in the severity of the crisis that faces the industry as a whole.

The financial crisis experienced by both the U.S. market as well as the reinsurance facilities, has resulted in a capacity shortfall of unprecedented proportions. It is estimated that approximately $67 billion of capacity will not be available for the remainder of 1985 on in to 1986.

Due to the financial concerns of many companies and the partial withdrawal of the reinsurance facilities, the U.S. market does not have the capacity to fill the insurance needs of everyone as they did in 1984 and previous years. The insurers are having to decide whether to place their remaining capacity in more at-risk lines or to place it in more traditional lines where they have been known to make a reasonable profit at less risk. The logic and reason behind withdrawal from the higher risk lines is due, in part, to the inability of the insurance companies to determine the potential costs of a risk for certain lines. For example, asbestos abatement contractors are having a tremendous difficulty in obtaining the necessary insurance in removing asbestos from public buildings and schools in various jurisdictions. Asbestos related illnesses have an extremely long latency period and may not be discovered for periods exceeding 20 to 30 years. It is difficult, if not impossible, to project with any degree of accuracy the costs that will be incurred for both the defense as well as potential liability payments 20 to 30 years into the future.

The financial crisis as well as the capacity shortfall has forced the companies to place their remaining capacity in less at-risk lines thus exacerbating the availability problems for the commercial lines. Day care facilities are not the only ones affected by this capacity shortfall in that we have a growing list which includes nurse midwives, obstetricians, neurosurgeons, municipalities and counties, long-haul truckers, facilities dealing with hazardous waste, dram shops, certified public accountants, architects and engineers, lawyers, rental car companies and so on.

The day care facilities have been caught up in this availability crunch and are being deemed higher risk, not necessarily based on a claims experience but due more to an insurance hysteria because of the adverse national publicity associated with child abuse situations. This is unfortunate in that the great majority of day care facilities are of excellent quality, very caring and devoted facilities who perform a needed and beneficial assistance to the many parents and children they serve. Unfortunately, the whole of the day care industry is being tarred with the same wide brush as those few centers that have actually participated in abuse of their children. The insurance industry has indicated in specific conversation with me that they feel it is a matter of time before the lawsuits come forth and this becomes a very volatile and explosive situation with the potential of costly defense and liability payments.

The National Association of Insurance Commissioners along with individual state jurisdictions are dealing with this crisis from several fronts.

Specifically, it is important to create an open dialogue with those insurance companies that are underwriting the day care facilities and attempt to separate the issues of child abuse from the normal liability aspects of this industry. Again, I suggest, we are not dealing with an industry-wide problem but a scattered instance of child abuse that has been blown out of proportion by the national media. We will hopefully be in a position of convincing those specific companies of the merits and necessity of continuing the needed coverages for the bulk of this industry.

In addition, it seems that policy provisions can be amended to exclude certain coverages if a particular day care facility is found to have participated in abuse of children. Insurance should not be available to those facilities involved in child abuse, and the insurance companies exposure should and can be limited in this area. Specific policy exclusions for child abuse will help restore the availability of liability coverages needed for the bulk of this industry to continue their programs. This will remain true as long as there is no judicial determination made to broaden the coverages not previously designed to cover certain excluded items.

Some of the state jurisdictions are individually exploring the feasibility of creating joint underwriting associations (JUA) to force the insurance industry licensed in those jurisdictions to write certain of these lines of coverages. JUA's historically have been noncompetitive arenas that solve the availability problem on a short-term basis but cause additional problems in seeking longer term solutions.

The NAIC and the individual commissioners have an expressed concern and interest to determine the appropriate solutions on a state-by-state basis. It is our intent to be part of the solution, and we will work toward the end as swiftly as possible.

We sincerely appreciate the opportunity to express these brief remarks and will stand available to respond to this committee with additional information and additional answers to questions that you might have.

Chairman MILLER. I think, given your time constraints, it may be better if we allow you to respond to these questions in writing, so that we can have time for other members of the Committee to question you.

Mr. MUHL. Very good. I appreciate that. I suggest to you, as well, not only will I respond to the individual questions, we are putting together an actual list of names of the companies that are still writing this business. We will be more than pleased to submit that to you and the committee and also to make that available to any of the day care facilities, not only in my State, but in any other jurisdiction for their use and information.

[The information follows:]

State of Maryland,
Department of Licensing and Regulation, Insurance Division,
Baltimore, MD, August 23, 1985.

Hon. **George Miller,**
Chairman, Select Committee on Children, Youth, and Families, House Office Building Annex 2, Washington, DC.

Dear Chairman Miller: I am returning the edited transcript of the hearing.

On behalf of the National Association of Insurance Commissioners and myself personally, I extend our thanks to you and your Committee in extending the invitation to appear and offer comment as to the day care facilities insurance situation.

You will find attached a brief listing also of those companies who are writing day care facilities insurance in Maryland.

With kindest regards,

Sincerely,

Edward J. Muhl,
Insurance Commissioner.

Attachments.

Current Survey of Major Underwriters Indicates the Following Insurance Companies and Brokers are Offering Liability Coverage for Day Care Centers:

FIREMAN'S FUND—(321-4700)

Property and Liability coverage for those affiliated with churches and schools; 5 covered now; not offering new business.

THE HARTFORD—(821-6000)

Renewing existing coverages. No new business.

U.S.F.&G.—(547-3712)

Not cancelling. No abuse exclusion. No new business.

NATIONWIDE—(224-3200, EXT. 310)

Adding abuse exclusion to existing coverages. No new business.

INSURANCE CO. OF NORTH AMERICA (CIGNA)—(215) 241-4000; 685-0300

Commercial package includes personal injury, excludes child abuse and sexual abuse. Will only insure groups, not private. Individual risk premiums.

TRAVELERS—962-6472

No new business. Renewing or non-renewing on an individual basis.

STATE FARM—(309) 766-2017; 662-5181

None for independent but will cover those affiliated with a church. Renewing old business. No abuse exclusion yet.

ALLSTATE—(312) 551-2491

Available.

ROYAL INSURANCE CO.—685-5844

No new business. Renewing existing business with abuse exclusion.

ZURICH-AMERICAN INSURANCE GROUP—(628-6500)

None offered to independents; only covering schools and churches. No abuse exclusion.

JEFFERSON INSURANCE CO. OF NEW YORK—(212) 683-4500

Write mostly independents that are small (less than 25 children) with abuse exclusion.

ST. PAUL FIRE & MARINE INSURANCE CO.—821-0210

No new business. Non-renewing high risk and small ones. Uses abuse exclusion.

NORTHBROOK PROPERTY & CASUALTY INSURANCE CO.—964-1800

Do offer; not actively seeking new business.

Brokers

L.E. HARRIS AGENCY, INC.—547-1552

General Liability, Owners/Landlords/Tenants, incidental malpractice and products coverage; exclude sexual abuse. Average $50 per child cost and $500,000 coverage limit. Coverage through Jefferson of New York and non-admitted companies.

HORAN, GOLDMAN & CO. OF MARYLAND, INC.—596-1115; 997-3845

General Liability only, but could do umbrella. Excludes child abuse. Policy minimum premium $500. Cost $30-$35 per child.

TONGUE, BROOKS & CO.—727-7172

Covers independents and groups through Mount Vernon Fire Insurance Company (a non-admitted company). Includes: Owner/Landlord/Tenant, premises liability, bodily injury, property. Can add miscellaneous professional liability and products coverage. Covers field trips. Exclusions: sexual abuse, constructural liability, autos, and mobile equipment. $½ million and $1 million limits.

(There may be other Insurance Companies and Brokers offering coverage as not all companies authorized to underwrite were surveyed. It should be noted that some of the Companies offer coverage on a limited basis.)

Chairman MILLER. Thank you. I certainly think that will be very helpful to people in Maryland and the surrounding areas.

Are you suggesting that when the midterm cancellations came through from the California company, to the policyholders in Maryland, that it was within your power as insurance commissioner to take certain actions? To condition other business that's being done in the State of Maryland to require that those cancellations not take place. Is that one of the regulatory powers that you have?

Mr. MUHL. On the regulatory powers that I have is with reference to a section referred to as the Unfair Trade Practices Act. Now, I have determined, as a result of a policy decision, midterm cancellation being an unfair trade practice. And I suggest that an insurance company has projected for the future what their costs were going to be and have actually entered into a contract with either an individual or a group.

Chairman MILLER. That was my next question. The underlying assumption there was that when the policy was written, certain financial decisions were made within the company to absorb the expected losses at that time out of that policy, and that was the agreement by which the contractual arrangement was entered into.

So I think not only does cancellation raise a very serious problem, it also represents the breach of a contractual arrangement, based apparently on a business miscalculation within the industry!

Mr. MUHL. That's right. Absolutely right. And if they guess right, they make a profit; if they guess wrong, so be it. But any rate request cannot make up for past mistakes or past losses; it has to be prospective only.

So I figure, they have collected the premium; they have made a commitment and if they do not fullfill that commitment, in my estimation, as in the estimation of a lot of my colleagues in various jurisdictions, that is deemed to be an unfair trade practice.

Chairman Miller. Do you know if there's movement by other insurance commissioners to reverse some of the midterm cancellations in other States?

Mr. Muhl. Yes; as a matter of fact, it's predominant throughout the various jurisdictions that they are heading in that direction. Not all States are but the bulk of them are, and I think there's going to be a move through the National Association of Insurance Commissioners to make that somewhat of a policy decision for the individual States to take back with them, and to employ that method of not allowing midterm cancellations nor midterm premium increases.

Chairman Miller. Well, I'm delighted to hear that. I can understand an industry that's in trouble. I just went through the longshoremen's coverage with the insurance industry and there clearly we understood that there was a problem, but it was also understood that coverage would be provided. In some cases, States put together pools to cover that problem, and we sorted it out.

We changed the policy that included unacceptable liabilities for the companies under that law. But there was a time to sort it out. We didn't put people out of business while we decided what we were going to do, and I think what has hit this committee so hard and has hit the child care industry so very hard, is the notion that you simply find in your mailbox a termination of a policy that in and of itself terminates your business.

We like to think we encourage responsible people to come to the child care industry, people who responsibly went out and bought themselves liability insurance to cover themselves and the children they take care of, and then on a given day they are out of business.

And I think that's what on the face of it is so offensive, and force us to look for the reasons, whether or not there's evidence to support the cancellations. Given time, I think we can sort the problems out. We are used to sorting out the complexities of those kinds of problems.

So I'm delighted to hear that you and other insurance commissioners are taking steps to buy some time.

Mr. Muhl. Well, I appreciate your saying that, Mr. Chairman, myself, as commissioner of Maryland, and I can say this on behalf of a lot of my colleagues and the National Association, as well, that we are very concerned about what is happening, not only to the day care folks, but what's happening in most of the commercial line. We have every intention to be an intricate part of the solution. And hopefully, as I say, we can move in that direction at a very swift pace.

Chairman Miller. Congressman Coats?

Mr. Coats. Mr. Muhl, thank you for your testimony. I am pleased that you not only are aware of the problem, but are actively taking steps to deal with it.

One thing that disturbs me a little bit is your testimony regarding insurance company capacity to carry certain lines of insurance. You've indicated a $67 billion shortfall in capacity. Now that, to me, suggests that even if you are able to accomplish the necessary dialog to write exclusions into the policies, that there is still a major problem existing in terms of providing coverage.

Could you elaborate on this capacity problem and what effect this might have on the ability to provide particularly renewals or expanded coverage in late 1985 or 1986 for the day care industry?

Mr. Muhl. You will have, at least from what I've seen, Mr. Coats, the list of those that will testify, some individuals from the industry who can elaborate on that, as well, but I suggest to you from the knowledge I have, yes, there are going to be a lot of people in various lines that will not be able to buy certain insurance coverage on the short term. Again, this is pretty much of an end of a cycle for the insurance industry, and it will get better.

There are going to be some companies that are going to fall out of the system, who have guessed wrong on the pricing of their products, and maybe they should fall out of the system. But at some point in time, hopefully in the very near future, the capacity is going to come back; the losses that are being experienced by the various companies are going to get back on their feet, if you will, and be able to expand that capacity.

Mr. Coats. Educate me a little bit here. Are you saying that if a certain company has a capacity problem, they are precluded from writing new insurance because of their reserve situation or whatever, regardless of what they might establish as a premium or a contract exclusion to narrow the risk?

Mr. Muhl. Each jurisdiction, specifically say in my case, Maryland, we require a minimum capital and surplus by law, and we require adequate reserves to cover any claims or future claim for that business they already have on the books. Now, if they are experiencing—I say, if they have guessed wrong on the pricing of that product—and they've lost money—we've had several companies domiciled in Maryland that lost some big dollars. One of our larger domestics last year had an underwriting loss of over $512 million, made up the bulk back in investment income, but still took a substantial loss. They do not have, as a result of that substantial loss, the capacity to expand into a new line, and in some instances, they do not have the capacity to continue certain lines that they're now insuring.

I suggest to you that there are some alternatives, though, to this. For an example, I've been talking to the Maryland Association of Counties and Cities; they are having a very very difficult time obtaining the necessary insurance. A lot of it is due to, again, being deemed high risk by the insurance industry. And in some cases, they are high risk. There are a lot of claims now being able to be brought against a municipality where at one time, they had a tremendous amount of governmental immunity.

That immunity has been eroded through various court decisions, and now you are seeing some of our small towns and cities in Maryland being sued for trips and falls on the sidewalk and things of this sort, they never had that exposure before. So it is very difficult for them to obtain the necessary insurance or, in some cases, to afford the insurance.

We have several of our municipalities and entities in Maryland who, many years ago went off into the direction of being self-insured by having in place a catastrophic cover, a catastrophic insurance cover. Now, this seems to be a very viable answer to a lot of our municipalities and small cities in Maryland.

Mr. **Coats**. Excuse me for interrupting here, but I don't think the day care industry is going to be able to pool resources or have access to resources that the municipalities can in order to provide self insurance.

Mr. **Muhl**. No; that's true. Now, the point I wanted to get at though, Mr. Coats, was that even though there's going to be a $67 billion shortfall in capacity, there are going to be some entities, such as the municipalities and others, who can find alternative mechanisms outside of the system of insurance. So it won't be as critical, if you will, as $67 billion.

That figure, I'm not sure what it would be, but when you take the entities out of the system that no longer then have the need for that capacity, the remaining capacity can be used elsewhere.

Now, with reference to the day care folks, we are very concerned; a lot of my colleagues are not only looking at alternative sources such as the possibility in some cases, if it's a larger association, in going self-insured, but looking at joint underwriting associations. These are ventures by the insurance industry where they would be in essence, forced, as a prerequisite of licensure in any given jurisdiction, they must accept *x* number of policies based on their total policy writings in that jurisdiction.

This is an alternative that we're exploring in Maryland and again, I suggest to you, that a lot of my colleagues are exploring the same alternatives in their individual jurisdictions.

So we are looking for the answers and I think we have some of the answers, but as time goes on, again, the capacity is going to come back as it has in the past.

Mr. **Coats**. But for a lot of child care centers, it appears the bottom line is that if I'm A B C Child Care Center, and I'm opening up for business here in 3 weeks to correspond with the school system, and I'm either a new entity or someone who has had their insurance cancelled or at least not renewed who goes into an insurance company. If I sit down with the company, and say, this is our experience. These are the statistics. We are willing to accept a higher premium. We're willing to write exclusions in the contract for sexual abuse and child abuse. It's very likely that the company could say, granted we wish we could write you the insurance; but, because of our loss experience in the past couple of years or our surplus and assets ratio to claims, we can't write the insurance.

I mean, isn't that the bottom line? Isn't that what a lot of child care facilities are going to hear?

Mr. **Muhl**. Yes.

Mr. **Coats**. And what are we going to say to them? Run the risk? Or self-insure?

Mr. **Muhl**. No; that very same question was asked me by some of the day care facility associations in Maryland and, to me, going self-insured for that particular group is an unacceptable alternative. And that's why we have made the policy decisions not to allow midterm cancellations. That's why we are considering a joint underwriting association to supply the availability.

We had this similar problem in 1973 and 1974 with the medical malpractice crunch that hit then. There were no insurance compa-

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nies left in Maryland to insure the doctors for medical malpractice. And the State legislature created statutorily a private company called Medical Mutual Liability Insurance Society whose sole function it was to insure the doctors.

And that was an acceptable alternative for them.

Mr. **Coats**. Is that under consideration?

Mr. **Muhl**. It is under consideration. As a matter of fact, again, I suggest to you going uninsured or self-insured, to me, for the day care facility, is an unacceptable alternative. And we are exploring every avenue and every possibility to make sure that they retain the insurance they need.

Mr. **Coats**. Are there any State statutes that obligate the day care centers to notify parents as to their insurability, amount of insurability, lack of insurability?

Mr. **Muhl**. Not that I know of.

Mr. **Coats**. It is strictly voluntary?

Mr. **Rowland**. Will the gentleman yield?

Mr. **Coats**. Certainly. I'm way over my time. I'll yield to the gentleman.

Mr. **Rowland**. You mentioned the Medical Mutual Insurance Co., I believe you said that was an acceptable alternative?

Is it not true that some of the Mutual Medical Insurance Co.'s are also experiencing difficulty now?

Mr. **Muhl**. In most jurisdictions, Mr. Rowland, except for the State of Maryland. We are very pleased and very fortunate that we have a very solvent Medical Mutual Liability Society that insures the doctors.

Mr. **Rowland**. But in other areas, they are having some problems?

Mr. **Muhl**. They are having some extreme difficulties.

Mr. **Rowland**. Just wanted to make that point.

Chairman **Miller**. Congresswoman Boggs?

Mrs. **Boggs**. Thank you, Mr. Chairman. Thank you for being with us. I apologize that I missed most of your testimony. I have a question that Dr. Rowland was proposing that came to my mind, as well. In reading over your letter to the chairman, I notice that the capacity shortfall has encouraged you to have difficulties with various kinds of insurance including nurse midwives, obstetricians, and day care centers. Isn't this really a very loaded situation for mothers and their children? Day care is probably the most important social and economic measure in our country today.

I can't believe that the insurance industry cannot in someway devise the kind of insurance coverage that can provide safe day care for the children of America—especially if the industry is having difficulty in providing insurance for the birth of the children, safe birth of the children, care of their mothers prior to their birth.

If indeed the decision of insurance companies not to enter into some kind of affordable insurance for day care centers is not based on claim experience, what is it based on?

Mr. **Muhl**. I suggest to you, as I did indicate earlier, that it's more of an insurance hysteria than it is a concern about actual claims or poor claims experience as to child abuse. The industry, for all intents and purposes, is waiting for the hammer to fall on a tremendous frequency if you will of lawsuits coming in. Again, because of this hysteria, because of the capacity shortfall that they have, and the poor experience that they have sustained over the past couple of years, 1984 being in essence the worst year ever losswise in the whole history of insurance.

And 1985 beginning to be at least looking that much worse than 1984. There is that hysteria. And they are looking at the possibility of just everything going a little crazy, with reference to lawsuits and the massive amount of money it will take to defend these lawsuits. So, they are placing that capacity into more traditional lines, less at risk lines.

Now, with that, I suggest to you that you are absolutely correct. There is little or no claims that have been filed on a national scale with reference to child abuse or sexual abuse of the children. So, it's again, more hysteria, than it is actual claims experience. Now, that's where I think that we can have the most inroads. I think the insurance industry has really missed the boat on this. I think that they can and should insure the day care facilities because I happen to agree with you totally. This is a very needed industry. It's a very caring industry. A good quality industry that supplies a tremendous service to us, as parents, and to our children.

It is unfortunate that we have a very small number of day care facilities being involved in this abuse of children, but you look at the national publicity that has come out as a result of just a very very few of these centers, a minority of these centers. I didn't realize that there were some small towns in California or Arizona, never heard of these names. And all of a sudden they're on the national news and on the front page of my local newspaper in reference to child abuse.

So, it's this hysteria. I think that the thing that we need to do, and the steps that the NAIC has taken, to create this dialog with the insurance industry to try to separate these issues, to show that, in fact, the claims experience is not there. Particularly, if we can put certain policy exclusions into the individual policies to make sure that the insurance companies are not at risk or exposed to sexual abuse or child abuse claims. But to be there to offer the insurance for other necessary liabilities that the day care folks need.

I think that's very important and I think we have made some inroads to that extent, and I feel somewhat confident that we can supply or at least cause the industry to supply the necessary availability. If not, there are these other alternatives that I was talking about, such as the JUA's and things of that sort.

Mrs. BOGGS. Thank you.

Chairman MILLER. Congressman Monson?

Mr. MONSON. Thank you, Mr. Chairman. If you answered this, I apologize, but I must have missed it if you did. Did you say that as far as midterm terminations go, that most states have the same policies that you have in Maryland?

Mr. MUHL. Most of my counterparts, Mr. Monson, in the other jurisdictions, have made policy decisions not to allow midterm cancellations nor midterm premium increases. Not all jurisdictions have made that because there are some restrictions in individual State laws. Some insurance commissioners feel they do not have the statutory authority to do that.

I suggest to you that I do not have in my laws in Maryland, the insurance laws, specific authority in dealing with midterm cancellations, but I have made the policy decision that this would be an unfair trade practice, and as a result, I will not allow midterm cancellations nor the midterm premium increases.

Mr. Monson. What happens at the end of the term? What are your alternatives at that point, not to renew a policy?

Mr. Muhl. That's a difficulty and that's a concern. That's one I do not have statutory authority to deal with. But by the time we get to that point, I'm very hopeful that we're going to have a longer term solution.

Mr. Monson. And most States are in that?

Mr. Muhl. Most States are in that situation, yes.

Mr. Monson. You indicated that one method of solving a situation similar to that with medical malpractice was for the state, did they create this private company, did you say, through legislation?

Mr. Muhl. Yes; in the State of Maryland we did create—as a matter of fact, we have two entities in Maryland that are somewhat unique: the one as a result of the malpractice crisis in 1973-74', created the Medical Mutual Liability Society to insure the doctors, and that is functioning quite well and it is solvent.

Mr. Monson. Are the reserves for that funded from State appropriations?

Mr. Muhl. No; it was an assessment, a general assessment of $300 for the doctors to get started to have the necessary capital, necessary surplus.

Mr. Monson. Did that provide enough reserves?

Mr. Muhl. It did. We have another facility that was also statutorily created, it's a little different than the Medical Mutual in that Medical Mutual is a private company. The State of Maryland has a very unique entity that is a State agency, the State of Maryland is, in fact, in the insurance business, and it's referred to as the Maryland Automobile Insurance Fund. And it's a facility of last resort for automobile coverages for anyone who cannot obtain the necessary insurance from the private sector. If they are turned down by the private sector, they can obtain the insurance through this facility.

And it is somewhat competitive.

Mr. Monson. Do you see any other options than those two for situations like we are talking about where insurance is required for them to be in business but they cannot obtain it through private companies?

Mr. Muhl. Do I see other alternatives? Well, let me say——

Mr. Monson. I assume that those two that you've just discussed are two alternatives?

Mr. Muhl. They are two of the several alternatives. I suggest to you that there are companies in a survey that my staff had conducted this morning and I just got that information over the phone. We surveyed 28 companies: 15 have elected no longer to stay in that line of business to supply insurance to the day care facilities. There are 13 still writing the business, and out of that 13 there are 3 that have no restrictions whatsoever and that are writing anybody in the day care facility or the day care group.

There are two that only write church-affiliated day care facilities; two others, group only; and six are renewing existing policies but not taking on new business.

So, there is a capacity out there. One of the other alternatives was this Market Assistance Program that I've referred to, and that is an assistance by and through my office in attempting to match up those day care facilities that are in need of the insurance and those insurance companies still having the capacity.

Mr. MONSON. Thank you, Mr. Chairman.

CHAIRMAN MILLER. Congressman Rowland? No questions. Congresswoman Johnson?

Mrs. JOHNSON. Yes, I have just a couple of questions. I thank you for your leadership in your State in this crisis, and I commend you on defining as an unfair trade practice cancellation of an insurance policy unexpectedly.

I wonder if in the course of your work, you have also looked at what's happening to pricing of these policies as well? Have you addressed the issue of scalping, along with intervening to prevent cancellations? Have you intervened in any way to also freeze premiums?

One of the things that's happening that is really terribly concerning us is that coverage is being reduced, deductibles are being included, exclusions are being written in, and premiums are quadrupling. I know of one example, a situation in which the coverage was reduced from $1 million to $300,000; the deductible was increased from 0 to $1,000; the exclusion for sexual abuse was written in, and premium went from $1,300 to $5,000.

For a small day care center, this is a catastrophe. To intervene and say you can't cancel is irrelevant; they can't buy. Have you done anything to also freeze premiums and prevent what may very well turn out to be scalping just about as brutal as any we've seen?

Mr. MUHL. Yes we have. We have reviewed that situation, and I suggest to you that the law that we have in Maryland is very similar to most of the laws in the various States, that says that rates cannot be excessive, inadequate nor unfairly discriminatory. And I suggest to you to into that spectrum the excessive and the inadequate, requires very much of a balancing act.

I have not frozen any of the rates for a number of reasons. Again, as I pointed out, we have an industry that has taken a severe beating as to losses, a lot of it self-inflicted, I might add, as a result of participation in cash-flow underwriting, but the fact remains that a lot of these companies have taken a rather severe loss, to the extent there are a lot of companies that are now on the NAIC watch list for solvency concerns.

As a matter of fact, there's about 342 companies nationally that we are looking at whose solvency is at question. Now, with that, when I suggest to you that our law says the rates cannot be excessive, it also says that they cannot be inadequate. We cannot allow an insurance company to charge an inadequate rate that's going to place them in a position of being insolvent in a short period of time, because that causes them a whole new set of problems with promises that were given to the policyholder to fulfill that promise at a given time, if they are not there, they do not exist, then the promises go unfulfilled.

Now, my staff does look at the rates and in this particular case, we look at them after they are filed because we have a file and use system in Maryland, and they test the data, they look at all the statistical information, to determine whether or not the rates are excessive, inadequate or unfairly discriminatory.

Now, a lot of the cost that you see, it's a combination of costs. The initial cost of an insurance policy which would include general inflation, cost as a result of general claims experience—not necessarily those involved with child abuse, but if there has been an increase in general liability claims, trip and fall or injuries to the kids in some fashion, while on the playground or something in that order—then that would be reflected in the data that we would ultimately approve for an increase in rates.

The big jump though is coming in as a result of the insurance companies not necessarily having a great deal of capacity on their own, who have to go out and reinsure. They have to go out and buy insurance. And one of the largest facilities in the reinsurance market would be Lloyds of London. That's probably the best known.

Now, Lloyds are——

Chairman MILLER. They apparently have got their own troubles.

Mr. MUHL [continuing]. Lloyds, through various treaties, and in some cases on an individual basis, through facultative reinsurance, is charging exhorbitant premiums to the insurance companies. And that is an expense that is passed through to the policyholder as cost for that insurance.

That's something that's not controlled by the individual jurisdictions, and I'm not sure if it can be controlled. But we have, I say, in some instances where Lloyds has indicated they are partially withdrawing from the American market, because they have taken their worse beating ever in their whole history, they are suggesting that now, if they're going to remain partially into some lines of this business on reinsurance treaties, that they're going to charge *x* number of dollars.

And if the insurance companies want that treaty, they're going to have to pay the premium.

Mrs. JOHNSON. Could I just interrupt you in the interest of time? I guess, the point of my question was, have you done any analysis of price increases in this market to track whether or not they are being influenced by increased costs of reinsurance or some other definable factor? Or whether, in fact, some price increases are in response to fear—I mean it might be well-motivated, but it might still be scalping. In other words, if there's not a definable cost increase that they're responding to, and there's not a body of known data that shows an increase in costs in this line, which to my understanding there isn't and no one's claimed there is, then I think we need to look at premium rises. We need to address those in the short term as well, in order to provide the timeframe.

And I just wondered if you've looked specifically at changes in premium costs?

Mr. MUHL. My staff has, but for those companies in Maryland, this is something that is not being done on a large scale, as nationally, but it's something that as chairman of the Commercial Lines Property Casualty D committee of the NAIC, this is something that we are going to suggest at the meeting we have upcoming in Syracuse that this be done—the survey be done on a national scale through the various states.

But I suggest that my staff have reviewed the various filings and we have again, we take our statutory charge quite seriously, and if we determine that a rate is excessive, or gouged if you will rate, that we will discontinue that rate.

Mrs. Johnson. One last question. I know that my time is limited and we have many other panels, but I did want to clarify. In your testimony, you talk about the possibility of developing exclusions of separating the issues of child abuse and normal liability aspects.

Do you think that in a sense, defining liability is a better direction to move in than creating some kind of reinsurance fund or liability pool or assigned risk fund, or whatever?

Mr. Muhl. I think at this point, on a short-term basis, any one single solution is not going to supply the need or solve the problem in total. It's going to be a combination of a lot of things.

And again, I suggest to you that is on a short-term basis. I'm very confident that this is more at this point in time a short-term problem. I see within hopefully the next year or two, the capacity returning to normal, and then the problem there would be solved.

There are some difficulties, some inherent difficulties, and I suggest to you that we were looking at a JUA or a statutorily created company to take this over and we are very seriously considering that. If we do that, again, that creates a whole new set of problems and it's something that we are weighing; something we are looking at but I think the problems will be solved, given time.

Mrs. Johnson. I would conclude, from that comment, that you would prefer that you act, rather than us?

Mr. Muhl. Oh, absolutely. [Laughter.]

Chairman Miller. Congressman Wolf?

Mr. Wolf. I do have a question that I wish to ask. I've read that the Trial Lawyers Association has said that one of the underlying problems with professional liability insurance particularly, and perhaps other kinds of insurance, is that insurance companies are making tremendous profits. That's one of the problems which was alluded to by Ms. Johnson about the premiums that companies charge.

Can you, as an insurance commissioner, comment on that? Do you have access to information about the amount of reserves that insurance companies have?

Mr. Muhl. Yes, I do. As a matter of fact, we have each and every company that is licensed in the State of Maryland under some very strict reporting requirements, financially, on an annual basis, as well as, in some instances, on a quarterly basis. I have a team of financial examiners whose sole purpose in life is to go into an insurance company to check for financial solvency, to look at the investments, to look at every aspect of the finances of a particular company.

Each of my colleagues in the various jurisdictions has that same capability and we are all tied into the National Association of Insurance Commissioners' early warning information system on the solvency detection of the various carriers. Yes, we do have access to that information; we do make use of it; we do look at the companies.

If you were to separate some of the things that are happening, let's take investment income, for an example. There is a tremendous amount of investment income that the insurance companies are getting as a result of taking the premium dollar and investing it, and getting that return.

One of the problems that we are faced with is that as a result of the high interest rates we had over the past couple years, we had the companies participating in this cash-flow underwriting where they were going out, and in my opinion, pretty much casting to the wind, good logic, commonsense underwriting, properly pricing their product for what the risk factor would be on those, and going out and grabbing the dollars because the investment return was fantastic.

That has come back to eat them alive at this point. Because now that the interest rates have fallen, they were getting a nice return on their money, now the losses are mounting and the losses are greater than the premiums that are being charged, which really eats into the investment income. So the bulk of the industry is taking a loss, even after investment income.

Sure, there are companies making money, and in some cases, when we look at some of the companies, they have some rather substantial surpluses. We have one company in the State of Maryland, for example, that's valued in excess of $8 billion, but that's one of the companies that I alluded to that took a rather heavy beating losswise. They lost $512 million this past year, and the investment income did not make up for that. So, when you look at the actual net value, and the net worth, the company isn't really worth all that much.

But they do have sufficient funds to pay claims if they were to come due, today. So, yes, I guess, in the short, the answer is, we do have access to the information; there are companies making money; and there are substantial number of companies that are not making money.

Mr. Wolf. The amount of money they are making is not a problem, then?

Mr. Muhl. No.

Mr. Wolf. Thank you. Thank you, Mr. Chairman.

Chairman Miller. Thank you, very much. It would be helpful if NAIC could give us a list of States that have taken similar action with respect to your own, in terms of forestalling the cancellations. Obviously, the committee is getting an awful lot of calls from people about this problem, and I think if the States have gone back and required the righting of this, then people who have had their policies canceled in those States ought to know that they have an opportunity to resubmit that coverage.

Mr. Muhl. Be more than pleased to submit that. As a matter of fact, I requested this information of the various jurisdictions within the past 3 weeks, and they are still coming in. When I complete that, I would be more than pleased to send it on to you.

Chairman Miller. You said at one point, in answering Congresswoman Johnson's question, that some of these losses were self-inflicted due to—and then I didn't hear the rest?

Mr. MUHL. Cash-flow underwriting.

Chairman MILLER. The what?

Mr. MUHL. Cash-flow underwriting.

Chairman MILLER. Which was?

Mr. MUHL. This means that instead of properly pricing the product, they reduced the price of that product to try to gain the market share or to try to get as much business in as they could by being cheaper than the next guy, taking the money and investing it for high yield. It worked well for a couple years, and then the interest rates dropped and then the floor fell. And now they are stuck with a lot of business that is underpriced business that they are not receiving a sufficient amount of premium to cover the cost.

Chairman MILLER. This activity may be completely unrelated to child care policies, right? They may have done that with respect to——

Mr. MUHL. I think it was widespread, in just about all the lines. But I suggest to you that maybe that is one of the problems I know the obstetricians, for an example, in Maryland, and in other jurisdictions are really concerned about now, their costs. In Maryland, there's not an availability problem at this point for the obstetricians. They are concerned about the cost.

Now, I think the rates were, in some instances, held artificially low for the last couple of years. Again, you had this grab for the policy premium and the policy dollar for the investment purposes, and the rates were sort of artificially held down.

Chairman MILLER. So the theory was that they could make up the difference in the real rate and the offered rate by putting the money to work at high interest returns?

Mr. MUHL. Yes.

Chairman MILLER. So with the speculation over, we're back to jacking up rates across the board in a number of fields, not just child care?

Mr. MUHL. And probably the most severe problem I've had in trying to explain why these rates have gone up has been to my wife who just paid our insurance bill for our automobile and she still doesn't believe me. And I tried to give her all the information and reasons why. But it's difficult for all of us.

But we're getting back to a point, now, Mr. Chairman, where the prices are coming back to where they probably should be and that's in some cases, a dramatic increase over the past couple of years. I guess a lot of us would have been in a better position if it were given to us in smaller doses instead of larger doses.

But I thank you, Mr. Chairman.

Chairman MILLER. Thank you very much. Your testimony has been very helpful to us.

Mr. MUHL. Thank you.

Chairman MILLER. The next panel that the committee will hear from will be made up of Mavis Walters, who is a senior vice president of the Insurance Services Office; Frank Neuhauser, Jr., who's vice president and actuary for AIG Risk Management; and James Kimble, who is the senior counsel for Federal affairs, the American Insurance Association. Welcome to the committee and we will hear from you in the order in which I called your name.

Your written statement will be included in the record in its entirety, and please feel free to summarize to the extent that you are comfortable.

Ms. WALTERS. Thank you very much, Mr. Chairman.

STATEMENT OF MAVIS A. WALTERS, SENIOR VICE PRESIDENT, INSURANCE SERVICES OFFICE

Ms. WALTERS. I am Mavis A. Walters, senior vice president of ISO. Insurance Services Office is a nonprofit corporation that makes available rating, statistical, actuarial, policy form and related services to any U.S. property casualty insurer. We are not a trade association, and we do not take positions on legislative activities. But on occasion, because we are a technical organization, we do serve as advisers to the industry, and hence, our appearance today.

We serve our participating insurers in a variety of ways, for 16 lines of insurance, including the personal lines which would include homeowners and personal auto, and the commercial lines of insurance about which we've heard a great deal, and I dare say, we'll hear a great deal more, today.

Our current commercial general liability program includes alot of sublines, again, some of which we discussed this morning. One of our sublines is owners, landlords and tenants' coverage or commonly called OL&T. That is the vehicle that is commonly used to provide liability coverage to day care centers.

As a statistical agent, ISO compiles data from the insurers who file their information with us. We have presented to you, on page 2 of my testimony, the actual experience for this class of business in our statistical plan that would be class 82115—the title of the class is day nurseries, but this does include the experience for child care centers. I'm certainly not going to read the table. I'll allow you to look at it and digest it. Let me see if I can try to explain what some of those numbers mean, very briefly, and obviously there will probably be questions. I'll be happy to answer them.

The table shows, for example, that for the first year, the one which we label policy year ended December 31, 1980. That very last column, Loss and Loss Adjustment Ratio, as you can see, it's 0.704. That indicates that just over 70 cents of every dollar of earned premium for this class of business was needed to cover losses and loss adjustment expenses.

However, 4 years later, by the end of policy year December 31, 1983, over $1.33 was needed just for losses and loss adjustment expenses for every dollar of premium earned. I should emphasize that these figures do not include any of the expenses in providing insurance during those years; it only includes the loss adjustment expenses. The general expenses involved in writing a policy, such as the acquisition costs and general expenses and premium taxes, et cetera, for this line of insurance, average about 35 to 40 cents on the dollar.

Clearly, I believe, this table demonstrates that the prices that were actually charged for this coverage for the most recent 4-year period have been insufficient to cover even the claims, much less the cost of doing business. For the total 4-year period, I've summarized in my notes the total premium collected for all coverage is about $11.7 million, but the total loss is for $12.2 million.

We had a great deal of discussion this morning about the current financial condition of the industry and the capacity shortage. Let me see if I can summarize briefly, in a slightly different fashion, what it all means. And I think it's terribly important to understand this so that we can put this problem in perspective, and as Commissioner Muhl discussed this morning, the problems are not limited to day care facilities.

Since 1980, losses and expenses have exceeded premiums primarily because prices failed to keep pace with loss costs. An unbroken string of underwriting losses began in 1979 and grew at an average annual rate of $8 billion through 1983. While the underwriting results have declined since 1979, the industry's net investment income has grown continuously. However, the average annual investment income growth of $1.7 billion did not even come close to the average growth of $8 billion for underwriting losses from 1979 to 1983.

In this regard, in fact, the commercial line's experience has been particularly terrible. General liability leads the pack with the highest combined ratio of 152. A combined ratio reflects not just the losses and loss adjustment expenses, but the actual expenses of doing business as well. A major factor contributing to these miserable underwriting losses and the tightening insurance market, are the excessive costs of the civil justice system which may also threaten the industry's ability to accommodate future insurance needs.

Recent court decisions have created new and uncertain liabilities for commercial line insurers. Another ingredient adding to that poor financial condition of the industry is the decline in policyholder surplus. If you will, policyholder surplus is the same as net worth for another corporation. Policyholder surplus is the term we use in the insurance industry. As a result of operating losses in 1984, industry surplus fell by $2 billion.

I would like to emphasize that this operating loss reflects the net of all the investment income earned and the underwriting losses. Underwriting losses were so severe that they gobbled up all of the investment income earned and produced an operating loss for the entire industry for 1984.

In late 1984, our organization, ISO, completed a study entitled "The Coming Capacity Shortage," which in fact Commissioner Muhl referred to earlier. In that study, we estimated that available property casualty insurance may fall short of demand by $62 billion over the next 3 years. I believe Commissioner Muhl misspoke when he said $67; it's really $62 billion. By the way, I do have copies of the capacity study which I'd be very happy to leave with you, Mr. Chairman.

We estimate that 91 percent or $56 billion of that 3-year shortfall would be in commercial lines. One of the problems adding to the difficulties, of course, again, as Commissioner Muhl mentioned, is reinsurers have suffered even more adverse results than the industry as a whole. It was clear to everyone that 1984 industry operating results are the worst ever and insurers must regain control of their basic business. Action must be taken in 1985 to insure return to profitability in insurance operations.

Significant premium increases are needed, especially for the commercial lines products. These necessary increases will not generate excessive profits, but will merely hopefully allow return to reasonable profitability after years of substantial underpricing. Earnings on funds invested in the insurance industry must be improved to maintain and attract the capital necessary to provide the capacity to meet the insurance demanded by our entire economy.

The gravity of the industry's financial situation and the need to strengthen loss reserves will exist for several more years, I'm afraid. Until premium increases begin to restore the industry to financial health, the hard market will create, indeed has created, a whole new set of problems for all of us. Some insurers may not survive; indeed, some insurers will not survive.

Others with a strong capital base should be able to prosper and serve a wider market. In preparation for meeting these challenges, some companies have already increased their capital base through stock or convertible debt securities offerings, capital markets thus far have responded positively, in my opinion because they believe that they are getting in on the ground floor of a recovery, and will be looking for positive earnings from insurers.

Given 1985's more challenging circumstances, recovery will require certainly responsible business decisions and the cooperation of knowledgeable consumers and insightful regulators.

Thank you, Mr. Chairman.

Chairman **Miller**. Thank you. Mr. Neuhauser?

[Prepared statement of Mavis Walters follows:]

PREPARED STATEMENT OF MAVIS A. WALTERS, SENIOR VICE PRESIDENT, INSURANCE SERVICES OFFICE

Insurance Services Office, Inc. (ISO) is a non-profit corporation that makes available rating, statistical, actuarial, policy form and related services to any U.S. property/casualty insurer. ISO is not a trade association and therefore does not routinely represent insurers in legislative forums. However, on occasion, we do serve as technical advisors to the property/casualty insurance industry and in that capacity may appear with trade association representatives before legislative bodies.

ISO has no mandatory membership requirements, nor do we have adherence requirements with respect to advisory rates, loss costs, policy forms or programs. In fact, we actively encourage independent action by participating insurance companies.

We serve participating insurers by gathering, storing, and disseminating statistical information to regulators, as required by law, and to insurers for their own use. We also develop and assist in implementing programs that help define and cover risk. We promulgate advisory rates or advisory prospective loss costs for sixteen lines of insurance including personal lines (automobile and homeowners) and commercial lines of insurance such as Commercial General Liability (CGL). ISO's current CGL program incorporates several sublines of coverage, one of which is known as Owners, Landlords, and Tenants coverage (OL&T). OL&T is generally the vehicle used to provide liability coverage to day care centers.

The table below represents the most recent countrywide experience available for those companies reporting premium and loss data to ISO for advisory ratemaking purposes. This data is reported in accordance with the requirements of the ISO Commercial Statistical Reporting Plan for the Day Nursery class of business

COUNTRYWIDE OWNERS, LANDLORDS, AND TENANTS LIABILITY INSURANCE, CLASS 82115—DAY NURSERIES

(All Companies Reporting to ISO)

Policy year ending	Total limits earned premium	Incurred losses[1]		Medical payments	Number of incurred claims	Loss and loss adjustment ratio
		Basic limits	Excess limits			
Bodily injury						
Dec. 31, 1980	$1,785,529	$983,150	$743,127	$30,779	168	0.704
Dec. 31, 1981	2,581,645	1,144,240	997,137	44,807	205	.847
Dec. 31, 1982	3,321,139	2,041,498	1,340,296	89,347	321	1.045
Dec. 31, 1983	3,995,362	2,864,361	2,332,868	119,021	427	1.331
Total	11,683,675	7,033,249	4,913,428	283,954	1,121	1.047

[1] Including all loss adjustment expense and developed to an ultimate basis.

This table shows that for the policy year ended 12/31/80 just over $.70 of every dollar of earned premium was needed to cover losses and loss adjustment expense. However, 4 years later—i.e. for policy year ended 12/31/83 over $1.33 was needed for losses and loss adjustment expense for each dollar of premium earned. These loss figures do not include the additional expenses in providing the insurance during those years. Expenses for general liability policies average about 35 cents out of every dollar.

In order to put the present day care liability insurance problems into perspective, it is necessary to understand the overall financial condition of the insurance industry today. Since 1980, losses and expenses have exceeded premiums primarily because prices failed to keep pace with loss costs and lagged the nation's overall economic growth. As a result, an unbroken string of underwriting losses began in 1979 and grew at an average annual rate of $3 billion through 1983.

An even more dramatic increase took place in 1984 when underwriting losses jumped $8 billion, reaching $21.3 billion. Losses from underwriting for the six years 1979 through 1984 totalled a staggering $55 billion.

While underwriting results have declined since 1979, the industry's net investment income has grown continuously. In an attempt to generate cash flow for investment, insurers competed aggressively for premium dollars, knocking prices more and more out of line with loss costs. However, the average annual investment income growth of $1.7 billion did not even come close to the average annual growth of $3 billion for underwriting losses from 1979 through 1983.

In 1984, the 10% increase in investment income of $1.6 billion was far below the 60% increase of $8 billion in underwriting losses. With investment income lagging far behind underwriting losses, the industry's pretax operating income—the combination of investment income and underwriting results—plunged to a negative $3.8 billion in 1984.

In this regard, the commercial lines experience has been particularly terrible. Four key commercial lines—General Liability, Commercial Multi-Peril, Workers Compensation and Commercial Automobile—are disasters. General Liability leads the pack with the highest combined ratio of 152.

A major factor contributing to these miserable underwriting losses and the tightening insurance market are the excessive costs of the civil justice system which may also threaten the industry's ability to accommodate future insurance needs. Recent court decisions have created new and uncertain liabilities for commercial line insurers. Such decisions, in fact, have rewritten terms of policies and altered the obligations of the insurers to their policyholders. In addition, legislative initiatives that liberalize the tort liability system have added to insurance costs.

Yet another ingredient adding to the poor financial condition of the insurance industry is the decline in policyholder surplus. Policyholder surplus is the difference between insurers' assets and liabilities and is a measure of an insurer's capacity to provide insurance coverage safely. As a result of operating losses in 1984, industry surplus fell 3% to $63.6 billion. In constant dollars, 1984 surplus was 3% below the 1980 level, which indicates that capacity may not be sufficient to meet the insurance needs of an expanding U.S. economy.

In fact, ISO has recently conducted a study entitled, "The Coming Capacity Shortage," which projects that the available property/casualty insurance may fall short of demand by $62 billion over the next three years. This projection is based on a fairly stable financial scenario which indicates that the capacity shortfall could be even more severe if circumstances are less favorable than assumed.

ISO estimates that, under reasonable assumptions, the capacity shortfall would be $7.2 billion or 5% of the market in 1985, $22.6 billion or 14% of the market in 1986, and 32.0 billion or 18% of the market in 1987.

Ninety-one percent or $56 billion of the three-year shortfall could be in commercial lines. The commercial lines shortfall would be $7.1 billion or 9% of the commercial lines market this year, $20.6 billion or 22% in 1986, and $28.3 billion or 26% in 1987.

Another element affecting capacity is that, in 1984, reinsurers showed much more adverse results than the industry as a whole. Reinsurers have tightened their underwriting and the reinsurance-capacity shortfall could be 25% of that potential market by 1987. The inability of primary insurers to obtain adequate reinsurance would further restrict their growth.

Due to the unique nature of the insurance industry's present cycle and the fact that the industry's current financial situation is much worse than any preceding cycles, a recovery will take longer, perhaps three years or more. This time, reinsurers have restricted their market and captives and self-insurance mechanisms are less likely to be effective safety valves. It is also less likely that additional industrial conglomerates or additional foreign entities will aggressively enter the insurance business over the next few years. The net result will be that premium-to-surplus ratios will rise dramatically, and a substantial capacity/insurance-availability problem looms on the horizon.

It is clear that 1984 industry operating results are the worst ever and insurers must regain control of their basic business. Action must be taken during 1985 to ensure a return to profitability in insurance operations.

Insurers must develop solid business products, and their prices must correctly reflect the costs and expenses for coverages provided. Significant premium increases are needed, especially for the current commercial lines products. The public must be made aware that the necessary increases will not generate excessive profits, but will merely allow a return to reasonable profitability after years of substantial underpricing. Earnings on funds invested in the insurance industry must be improved to maintain and attract the capital necessary to provide the capacity to meet the insurance demanded by our economy.

The gravity of the industry's financial situation and the need to strengthen loss reserves will exist for several more years, until premium increases begin to restore the industry to financial health. The hard market will create a whole new set of problems, testing all segments of the industry and regulation alike. Some insurers may not survive. Others, with a strong capital base, should be able to prosper and serve a wider market. In preparation for meeting these challenges, some companies have already increased their capital base through stock or convertible debt securities offerings. The capital markets have responded positively. Given 1985's more challenging circumstances, recovery will require responsible business decisions and the cooperation of knowledgeable consumers and insightful regulators.

STATEMENT OF FRANK NEUHAUSER, JR., VICE PRESIDENT AND ACTUARY, AIG RISK MANAGEMENT, INC.

Mr. NEUHAUSER. I appreciate the opportunity to testify before the select committee this morning.

Over the past few months, I have been involved in investigating the current problem shared by many child care providers in obtaining adequate affordable insurance. Our research has included: the experience of child care providers as a class; the underwriting criteria employed in underwriting individual child care providers; implications of the massive publicity of abuse incidents on insurance availability; and possible solutions to the current problem.

Over the past 6 years, the insurance industry has been submerged in the most prolonged unprofitable period in its history. Limited information is currently available on the experience for child care providers. The data that is available, however, does not indicate that child care providers as a class of insurance are any worse or better than average.

One particular problem with insurance for child care providers is that much of the insurance has been written for associations through managing general agents. Over the past few years, associations, in general, through leverage, produced from generating large premiums, have been able to command reduced premiums and less selective underwriting. Association business, as a result, has been cited as a major contributor to the failure of specific insurance companies. Managing general agents who produce most association business previously enjoyed broad latitude in the authority granted to them by insurance companies. This authority has been curtailed or completely eliminated over the past year.

Our researchers determined that the insurance industry relies heavily on underwriting judgment in evaluating exposure for child care providers. Included in the criteria, are: whether the child care provider is licensed; specific licensing standards and the enforcement thereof; child staff ratios; screening process for employees; physical condition of the facility, whether the facility was originally intended for child care or was converted from some other use; the transportation of children by the child care provider; food preparation; and available medical facilities.

The variation between one child care provider from another based upon the aforementioned and possibly additional criteria, can be extremely significant. As such, adequate selection processes become a heavy administrative expense for insurance companies. Considering the low average premiums, at least historically, the relation between administrative expense and collected premium would appear to be prohibitively high.

The current unprofitability withn the insurance industry has led to severe shortages for a variety of insurance coverages. The insurance industry as a whole is concentrating on avoiding exposure to risks which have caused severe losses in the past or have the potential to cause severe losses in the future.

It seems that every week we see headlines detailing cases of physical or sexual abuse of children in child care facilities. The potential for multimillion dollar judgments does exist. To my knowledge, no million dollar award has ever been paid in a child abuse case. Awards of over $1 million, however, have been paid under ludicrous situations. What would a jury that awarded $1.2 million to an overweight man who had a heart attack due to the force required to start a lawnmower, award to a child who has been scarred for life by intentional malicious abuse?

To a great extent, the problem in obtaining insurance for child care providers is part of a much greater problem. Many of us believe we are living under a court system that is completely out of control. The impact of the current escalation in judgments makes the underwriting of any liability insurance a risk that is not only potentially expensive in the current year, but provides a latent exposure for decades to come.

In a sense, child care providers expose an insurance company to potential losses in the same manner as chemical and pharmaceutical manufacturers. Decades ago, the insurance industry did not envision the extent of the damage that was being done by asbestos or DES. As a result of the escalation of awards for damage to people from numerous cases—drugs, chemicals, medical malpractice, for example, insurance companies are reluctant to provide coverage. As a result of past experience with chemical and pharmaceutical manufacturers and distributors, these industries have had extreme difficulty in obtaining coverage.

Again, it must be reiterated, that the insurance industry has seen its capital base erode over the past number of years. The insurance industry capital base or surplus can be equated to supply in an economic sense. Over the past 12 months, the insurance industry has seen demand for the first time in years exceed supply. The supply is being directed toward areas that would appear less likely to cause severe losses in the future.

The fact that available statistics do not indicate child care providers to have been in a group with losses of the magnitude of asbestos manufacturers or certain pharmaceutical companies, does not rule out this potential for the future. Similarly, the failure to identify large child abuse claim payments does not rule out this situation in the future. Many in the insurance industry expect that large judgments will be commonplace for child care providers.

Today's tort system not only produces large awards; it encourages them. The other morning while I was riding to work, I saw next to a bank advertisement a picture of a terrible auto accident with bold letters, "AN ACCIDENT LIKE THIS SHOULD NEVER HAPPEN TO YOU. BUT WHO WOULD YOU CALL IF IT DID?" The law firm of Brae & Rybicki P.C.—because you never know when it could happen to you. I've seen similar advertisements for malpractice.

Any long-term solution to the problem of obtaining adequate affordable insurance for child care providers requires an effort in a much broader arena. The primary problem clearly appears to be the application of our tort system. Unlimited contingent fees, punitive damages, and skyrocketing compensatory awards have not only affected the insurance product, but our entire economy as well.

Much has been written about our tort system inhibiting the development of new products and drugs. Even more relevant, we should consider the potential economic impact of inhibiting working single parents and two-income families from earning a living.

There are potential short term insurance and insurance related fixes: exclusions for physical and sexual abuse; stricter licensing and enforcement thereof; lower limits of liability; no-fault benefits as for workers' compensation; or claims-made policies.

Short-term fixes, however, will not provide us with what many of us believe to be necessary. Any permanent solution will require changes in our tort system.

As quoted in a recent Forbes article, "A World Without Insurance?" "No longer do we have the luxury of pretending the monster we have created will go away. It won't."

Thank you very much.

Chairman MILLER. Thank you. Mr. Kimble?

[Prepared statement of Frank Neuhauser follows:]

PREPARED STATEMENT OF FRANK NEUHAUSER, JR., M.A.A.A. VICE PRESIDENT AND ACTUARY, AIG RISK MANAGEMENT, INC.

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(1) The experience of child care providers as a class;

(2) The underwriting criteria employed in underwriting individual child care providers;

(3) Implications of the massive publicity of abuse incidents on insurance availability; and

(4) Possible solutions to the current problem.

Over the past six years the insurance industry has been submerged in the most prolonged unprofitable period in its history. Limited information is currently available on the experience for child care providers. The data that is available, however, does not indicate that child care providers, as a class of insurance, are any better or worse than average.

One particular problem with insurance for child care providers is that much of the insurance has been written for associations through managing general agents. Over the past few years, associations, in general, through leverage produced from generating large premium, have been able to command reduced premiums and less selective underwriting. Association business as a result has been determined to be more unprofitable than average and has been cited as a major contributor to the failure of specific insurance companies. Managing general agents, who produce most association business previously enjoyed broad latitude in the authority granted to them by insurance companies. This authority has been curtailed or eliminated over the past year.

Our research has determined that the insurance industry relies heavily on underwriting judgement in evaluating exposure for child care providers. Included in the criteria are:

Whether the child care provider is licensed;

The specific licensing standards and enforcement;

Child-staff ratios;

The screening process for employees;

The physical condition of the facility;

Whether the facility was intended originally for child care or was converted from other use;

The transportation of children by the child care provider;

Food preparation; and

Available medical facilities.

The variation between one child care provider from another based upon the aforementioned and possibly additional criteria can be extremely significant. As such, adequate selection processes become a heavy administrative expense for insurance companies. Considering the low average premiums, at least historically, the relation between administrative expense and collected premium would appear to be prohibitively high.

The current unprofitability within the insurance industry has led to severe shortages for a variety of insurance coverages. The insurance industry as a whole is concentrating on avoiding exposure to risks which have caused severe losses in the past or have the potential to cause severe losses in the future.

It seems that every week we see headlines detailing cases of physical or sexual abuse of children in child care facilities. The potential for multi-million dollar judgments exists. To my knowledge no million dollar award has ever been paid in a child abuse case. Awards of over a million dollars, however, have been made under ludicrous situations. What would a jury that awarded $1.2 million to a overweight man who had a heart attack due to the force required to start a lawnmower award to a child who has been scarred for life by intentional malicious abuse?

To a great extent the problem in obtaining insurance for child care providers is part of a much greater problem. Many of us believe we are living under a tort system that is completely out of control. The impact of the current escalation in judgements makes the underwriting of any liability insurance a risk that is not only potentially expensive in the current year but provides a latent exposure for decades to come.

In a sense, child care providers expose an insurance company to potential losses in the same manner as chemical and pharmaceutical manufacturers. Decades ago the insurance industry did not envision the extent of the damage that was being done by asbestos or DES. As a result of the escalation of awards for damage to people from numerous cases—drugs, chemicals and medical malpractice, for example—insurance companies are reluctant to provide coverage. As a result of past experience with chemical and pharmaceutical manufacturers and distributors, these industries have had difficulty in obtaining insurance.

Again, it must be reiterated that the insurance industry has seen its capital base erode over the past number of years. The insurance industry capital base or surplus can be equated to supply in an economic sense. Over the past twelve months, the insurance industry has seen demand, for the first time in years, exceed supply. The supply is being directed toward areas that would appear less likely to cause severe losses in the future.

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Any long term solution to the problem in obtaining adequate affordable insurance for child care providers requires an effort in a much broader arena. The primary problem clearly appears to be the application of our tort system. Unlimited contingent fees, punitive damages and skyrocketing compensatory awards have not only affected the insurance product, but our entire economy as well. Much has been written about our tort system inhibiting the development of new products and drugs. Even more relevant; we should consider the potential economic impact of inhibiting working single parents and two income families from earning a living.

There are potential short term insurance and insurance related fixes:

Exclusions for physical and sexual abuse;
Stricter licensing and enforcement thereof;
Lower limits of liability;
No fault benefits as for workers' compensation; or
Claims-made policies.

Short term fixes, however, will not provide us with what many believe is necessary. Any permanent solution will require significant changes in our tort system. As quoted in a recent Forbes article, "A world without insurance?" "No longer do we have the luxury of pretending the monster we have created will go away. It won't".

Thank you.

STATEMENT OF JAMES L. KIMBLE, SENIOR COUNSEL, FEDERAL AFFAIRS, AMERICAN INSURANCE ASSOCIATION

Mr. Kimble. I'm Jim Kimble. I'm senior counsel for the American Insurance Association. The American Insurance Association represents 177 stock property and casualty insurance companies.

The scenario which presents itself today is one of a market in transition, not necessarily a market in panic or hysteria. Clearly, the statistical information provided by the Insurance Services Office suggests that rate increases are appropriate. They don't suggest, however, that the insurance industry should abandon the market.

The loss ratios are very similar to other loss ratios in the general liability area. Those statistics suggest prudence, not panic.

Indications are that market adjustments are taking place. As some carriers have left the market, other carriers have either expanded their coverages or have entered the market. For instance, in California, we know that there was one company which provided a great deal of the coverage in that State. They were forced to curtail their coverages, and we know of at least three companies in your home State which have moved into that market. Now, perhaps, that coverage isn't enough to offset the one company which left the market but, hopefully, that sort of market movement by other insurance companies will accelerate, and any shortfall will be made up in the near future through these other companies entering the market or expanding the amount of coverage which they're offering.

What we'd like to suggest to you today is that any approach to solutions be phased in. Clearly, the first approach which should be initiated is for this committee and the State insurance commissioners to act as facilitators.

I believe there is some degree of misunderstanding between the two involved or affected industries. My people are, to some extent, a little confused about the lack of regulation and standards for the day care industry. We've heard testimony from day care owner/operators suggesting that because they have had no claims, they don't understand why their premiums are increasing.

That clearly suggests that they don't understand very basic insurance principles associated with spread of risk. I would suggest that this committee act as a facilitator and open a room so that the two affected industries can sit down together and hopefully create a better level of understanding.

Also, market assistance programs are being mentioned. That is a good voluntary, private sector approach to linking up insurers and insureds. Hopefully that will be enough of a solution. If necessary, State insurance commissioners and State legislators will go beyond that. We've had references to joint underwriting associations made today. That also is a potential solution. Not one that the insurance industry would look favorably upon, necessarily, but it does clearly indicate that coverage will be made available.

But I'd like to emphasize that the first step should be voluntary private sector solutions, an attempt to increase the level of understanding between the two industries, and a voluntary effort to link up policyholders with insurers.

Thank you.

[Prepared statement of James Kimble follows:]

Prepared Statement of James Kimble, Senior Counsel, American Insurance Association

The American Insurance Association (AIA) is a trade association which represents 172 property and casualty insurance companies. The member companies of the Association provide a majority of the commercial line insurance coverages written throughout the United States. Some of AIA's members provide general liability coverage to professional day care centers. Liability insurance is provided to some family day care homes through the application of the "business pursuits" endorsement which removes the business exclusion from the homeowner's policy.

Professional day care centers and family day care homes are currently experiencing a liability insurance availability and affordability problem. To the extent that state law mandates the acquisition of general liability insurance coverage as a prerequisite for doing business, the availability/affordability situation is exacerbated. Current insurance market conditions for professional day care centers suggest a market in transition rather than chaos. The countrywide experience for those companies reporting premium and loss data to the Insurance Services Office, Inc. (ISO) for advisory ratemaking purposes for day nurseries appears to conform with the current loss experience for the majority of commercial insurance lines. If expense factors are built into the loss and loss adjustment data for day care nurseries provided by ISO, the combined ratio approaches the aggregate general liability combined ratio of 152. Although these losses clearly indicate the need for increased rates, they do not suggest that insurers should abandon the market.

Insurance availability and affordability problems are not confined to the day care industry. Societal litigiousness and our legal system's movement towards the notion of absolute entitlement has resulted in availability/affordability problems for commercial automobile insurance, pollution insurance, municipal liability insurance, and professional liability insurance. Recent publicity associated with sexual and physical abuse in day care centers and homes may, in the judgment of the insurance industry, result in increased frequency and severity of claims. This increased publicity, coupled with the possibility of standards of absolute liability being applied in an area as sensitive as child care, serves to increase the underwriter's caution.

The weakened financial condition of the insurance industry and the increased demand on insurers' capacity to provide insurance coverage has impacted all lines of insurance. Since 1980, losses and expenses have exceeded premiums. In 1984, the property and casualty insurance industry experienced underwriting losses of $21 billion offset by investment income totalling $17 billion, resulting in a drain on insurance industry surplus of approximately $4 billion. Diminished surplus and the resulting shortfall in the industry's capacity to respond to the increased demands for insurance will affect the availability and affordability of all commercial lines, including general liability for family day care homes and professional day care centers.

Liability resulting from criminal acts has traditionally been excluded from the general liability policy. More recently, sexual and physical abuse has also been excluded from the policy. However, judicial misinterpretations of insurance contracts have altered the obligations of insurers to their policyholders and have resulted in liability exposures which were never contemplated by the insurer and for which no premium was collected. Specific to day care centers, plaintiff attorneys have finessed the criminal and sexual or physical abuse exclusions by claiming negligence in hiring practices. Judicial interpretations which make coverage available through tortured decisions has further added to the degree of prudence displayed by underwriters.

An expeditious solution to the current market displacement problem must come voluntarily from the private sector. Coordination between representatives of the insurance industry and family day care homes and professional day care centers is necessary in order to identify potential insurance markets and policyholder groups. As insurers restrict their writing for day care centers, others may aggressively enter the market to replace that coverage. A better mutual understanding of the problems of the two affected industries will enhance the process of linking insurers with insureds. This voluntary approach to solving the insurance availability/affordability problem should be given a chance before state or federal legislators attempt to address the problem through legislation.

NOTE.—This statement has been endorsed by the Alliance of American Insurers.

Chairman MILLER. Thank you very much.

Ms. Walters, let me ask you a couple questions with respect to the table on page 2. In 1980, you had total premiums of 1.7 and in 1983, you had total premiums of 3.9.

Now, let me ask you, that is not for the same number of facilities nor the same number of children, is that correct?

Ms. WALTERS. That's correct.

Chairman MILLER. I assume that reflects both an increased number of policies and some policy rate increase?

Ms. WALTERS. That's correct.

Chairman MILLER. During that period of time, you indicate for the premium dollar earned, 70 cents was the expense paid out? I maybe phrasing that wrong.

Ms. WALTERS. Loss and loss adjustment expenses. That's what was paid in claims.

Chairman MILLER. So for every dollar in premium that was earned, 70 cents was paid out. Now, that 70 cents does not reflect what I think you referred to before as net operating loss. There is no investment income included in that. That simply was whether or not the premium dollar covered the loss?

Ms. WALTERS. Exactly.

Chairman MILLER. What was the investment income in 1980?

Ms. WALTERS. The investment income is certainly not calculated by individual class or even by line of insurance but we can give you figures for investment income in total for all lines of insurance. A.M. Best compiles these figures.

I can certainly tell you that, as I did indicate for the latest year in 1984, the sum of investment income and underwriting produced an operating loss.

Chairman MILLER. I understand that. I'm trying to determine what's happened in——

Ms. WALTERS. If you want to know it I have the figures for investment income as a percentage of earned premiums starting in 1951 through 1984, and the year we're looking at, in 1980, as a percentage, investment income as a percentage of earned premiums was almost 12 percent of earned premium in 1980, this is for all lines combined. In 1980 the underwriting loss was 3 percent of earned premium so that the operating income was 8 percent of earned premium in 1980.

Chairman MILLER. What I'm trying to determine is how and to what extent the industry sorts out whose shoulders the burden for making up the loss will fall. As the previous witness indicated, some of this loss might be self-inflicted. The problems with Firemen's Fund are not related to day care coverage. They're related to massive internal management problems and investment decisions that had been made, underwriting decisions that had been made. I think that is why people who have never had a loss on their policy ask, why me?

And I think that when you look it doesn't seem to me that the shortfall in the industry or the bottom of the cycle as you call it is going to be made up on the backs of nurse midwives or obstetricians, long haul truckers, and day care operators. That's not going to work. There's not enough premium there if you took every dollar they had in their pocket.

So how does the industry sort out these decisions? It's suggested by Mr. Neuhauser that these operators don't look any better or any worse than other people you insure. Why the cancellations here as opposed to other lines?

Ms. WALTERS. You've asked several questions.

Chairman MILLER. Yes.

Ms. WALTERS. Let me see if I can address them in any in the—

Chairman MILLER. You know more about your industry than I do, and I'm trying to figure it out with your help.

Ms. WALTERS. I believe Commissioner Muhl made the point that is terribly important in this line of insurance or in any other line of insurance to recognize that the history leading up to where we are today results in the fact that the premiums charged in the marketplace have not been sufficient to keep them current or in line with loss costs.

Indeed, the first principles of ratemaking are that the premium should be sufficient to cover all losses and expenses expected to be incurred under that policy contract. This is how ratemaking formulas are constructed. The whatever you want to call it—I would not have used the same terms as Commissioner Muhl but let's say the excessive competition of the eighties led insurers to abandon the discipline of pricing in line with loss costs.

Now, some may see that as an evil; some may see that as a good. I make no qualitative judgments; the fact is, the prices charged in the marketplace were inadequate. Insurers made those decisions because the managements, by in large, of companies believed that any shortfall, if you will, between premiums and expected incurred losses, could be made up through investment income because interest rates were running very high.

Chairman MILLER. Is it the expectation of the industry that the losses that need to be made up are the loss adjustment ratio, or do we have to make up for bad investment decisions?

Ms. WALTERS. No sir. Not the latter. Most definitely, most definitely not the latter. Let me see if I can——

Chairman MILLER. Then I'd be terribly concerned that you had a net operating loss of $3 billion?

Ms. WALTERS. That was——

Chairman MILLER. Because if you'd put aside my 30 cents in 1980, I might be better off in 1983.

Ms. WALTERS. Well, you didn't have 30 cents in 1980, because it still costs more to—the premiums charged in 1980 were still insufficient to cover the losses.

Chairman MILLER. But I'm trying to determine the universe of loss that I'm expected to cover with my premium dollar. It's not quite clear to me. It's not 70 cents, right? Because then there was the cost of writing it?

Ms. WALTERS. That's correct.

Chairman MILLER. So I've got to take in the overhead.

Ms. WALTERS. So add another 35 cents. Add another 35 cents for that and you can see, even in 1980, the combined ratio as you would then call it would have been about 105, if the combined ratio is 100, then losses and expenses were perfectly in line with loss costs, the company would receive no profit for writing the business through the underwriting, but losses and expenses would have been perfectly in line with loss costs. That's how you read the numbers.

Commissioner Muhl made another important point which I'd like to emphasize.

Chairman MILLER. Why the cancellations in this field, though?

Ms. WALTERS. Let me try to emphasize what I tried to emphasize at the beginning of my——

Chairman MILLER. The numbers don't explain to me the rash of cancellations in this field, as opposed to others.

Ms. WALTERS. I certainly for one, Mr. Chairman, I'm not going to sit here and defend midterm cancellations. I'll leave that to my colleagues from the companies and trade assocations, so I'm not going to defend midterm cancellations.

Let me try to put this problem in perspective. In our capacity study, we've tried to make it very clear—Mr. Neuhauser referred to it—we're talking about questions of supply and demand. They are no more complicated in the insurance industry than they are in any other industry, frankly. We are seeing that demand for insurance is going to fall short of supply. Now, we can quibble about to what extent these numbers will come up, but clearly, demand is falling short of supply today, and I'm afraid, no good news here, we project it's going to get worse before it gets better.

Why is that happening? It's happening because of the scenario that I laid out for you. This industry on a cash flow basis lost money in 1984; its surplus declined. In conducting the insurance business, there have been no profits to add to surplus which allows a company to continue to grow in terms of the premium volume it writes; to keep up with the needs of an expanding American economy. That hasn't happened. That's the only reason I was explaining those numbers, to put it into perspective.

For this particular class of business, I share the views as expressed by Mr. Kimble, to some extent. I don't see this as—I'm an actuary; I'm not an underwriter and our organization does not write insurance—but from my perspective as, let's say, a technical observer of the insurance industry, I don't see this class of business as having the same kind or potential for catastrophic losses as we would see in the medical malpractice area, for example, or in pollution liability areas. Frankly, those are questions that the answers are perhaps even beyond the imagination to delve into.

I don't see that same problem here. I think we may be by large dealing with transition problems. When supply falls short of demand, a prudent manager, whether you're running a grocery store or whether you're running an insurance company or an auto manufacturing plant, when supply falls short of demand, you look to make available that limited supply to those areas where you, as the manager or the chief executive offer, believes you are more likely to have an opportunity to earn a profit that will contribute to surplus, that will allow your surplus to grow, so that you can continue to provide insurance and in fact meet the expanding needs of an American economy.

Chairman MILLER. But the question remains unanswered for the Committee for the time being. So far, nobody has come forward suggesting this is a horrendous industry to provide coverage for. We don't know if there is a rational adjustment in premiums underway, and I share the concerns of Congresswoman Johnson about scalping in the premiums.

Is this industry one of those areas where you can put your dollars and make a profit? Maybe it is. But no rational sorting out of the cycles and the liabilities has taken place. So far, there's not a shred of evidence that that's what's taken place at all.

There was a decision, and I think Commissioner Muhl put it more succinctly, an hysterical decision based upon some newspaper articles, to change policy. So we don't know in an actuarial sense, if there was a rational adjustment in premiums, whether this is one of those areas that could still be covered. We're told simply that this is not one of those areas.

Ms. WALTERS. Well these data make it perfectly clear to me, as an actuary, that the premiums that have been charged in the most recent past have been too low, for whatever the reason, they've been too low.

Let me give you a simple example. If in the competitive environment, in the rush to gain market shares as was described before, an underwriter's judgment that the proper rate is, let us say, $1,000, that's the proper price to insure this product but because of the excessive competition there was a 20 or 30 percent reduction. Say, no, some other underwriter or agent comes in and says I'm going to write that business for $700. A 30 percent reduction.

To get—and that has gone on for the last 3 or 4 years in general for the commercial line of insurance—either, in fact, not even a holding pattern with respect to commercial lines, but indeed reductions over the years. That means that even to get back to the point where you should have been when you started, it takes excessive increases that are perhaps doubled. For example, a $100 premium reduces by 50 percent, it takes 100 percent increase to get back up to $100. So that the prices to get them back up to where they should be just to cover the losses and expenses, not to make up or recoup for past losses—that is not permitted and it's not allowed and it's not part of any rate-making structure, it's going to take several successive increases just to get that back where it should have been.

Insurance companies must file and ISO, as a rating organization, files rates with each jurisdiction, with each state or District of Columbia, for its classes each year, and we file for rate increases. And, as Commissioner Muhl indicated, those increases are scrutinized and approved by state insurance departments.

We are seeing these great increases because the starting point by in large was not the suggested or advisory manual rate which ISO has had on its books, but something below that so while we may file for modest increases of 10 or 15 or 20 percent, when they're starting way down here, they're going to take big jumps to get back where they should be. I think that's part of the problem.

Chairman MILLER. Congressman Coats?

Mr. COATS. Thank you, Mr. Chairman. Mr. Neuhauser, based on your testimony—and I just want to pursue this maybe I'm misreading it—but it seems to me that perhaps you're coming down a little bit differently than the other two witnesses in terms of the potential long-term risk. I'm referring specifically to your statement that says, "Many in the insurance industry expect that large judgments will be commonplace for child care providers in the future." This is a question that's been before us in both insurance hearings that we've had —the difference in expectations.

We know that the actuarial experience is not enough to justify it—perhaps enough to justify premium increases, but not to justify cancellations and the kind of extreme responses that we've seen from the industry.

I would like you, if you could, to elaborate on that statement that you made about the potential long term liability. Is it out there? Does it exist? Or is it just something that's in the minds of some of the underwriters because of the headlines they've read, and so forth?

Mr. NEUHAUSER. I think the potential is out there. But by the same token, I can agree that it minds. The potential for huge judgments for DES or asbestos, 20 years ago, was not even in an underwriter's mind. When we read about a child abuse situation and consider the potential impact on that child when that child reaches its majority, that potential is there. Similarly, and the insurance company for years has refused to insure the health hazzard of tobacco companies. To my knowledge there has never been a single penny paid for a health claim against a tobacco company.

There is that similar expectation that has been made by insurance companies. Now, as an actuary having reviewed the numbers, having searched to see if there were child care abuse cases that were serious in dollar magnitude, I could not find them. Having spoken to underwriters, having spoken to brokers, the expectation of large claims exists.

Mr. COATS. Is it not possible for the company to write an exclusion into the contract that will remove them from liability, or do you fear that the courts will not honor that exclusion?

Mr. NEUHAUSER. Frankly, sir, they feel that the courts would not honor that. The courts have taken some very difficult stances, at least as respects the insurance industry, on interpretation of coverage. Asbestos is a specific example where a coverage was written based upon claims, theoretically occurring during a year; limits of very small amounts were provided in the 30s and 40s.

The courts have made decisions in the *Keene* case or in the *Raymark* decision in Illinois, that those limits can pyramid and that anytime any insurance company had a policy out there, they can be gobbled up. So the expectation by many in the industry as respects the courts, is one that the courts will take the interpretation that will generate the large amount of money from the insurance companies.

Mr. KIMBLE. There's also the belief that both the criminal exclusion and the sexual and physical abuse exclusion can be finessed simply by claiming negligence in hiring practices. So you may have some sexual abuse claims buried under the rubric of negligence in hiring practices.

Mr. COATS. These kind of responses indicate to me that perhaps we have more than just a short-term sorting out problem in the industry. Due to losses and management decisions in all underwriting situations, the problems are much broader than the narrow scope of child care coverage.

The essential question remains: are we dealing with a short-term broad based sorting out problem, or are we dealing with a longer term situation that we also have to study?

Ms. WALTERS. Let me just throw in one thing Mr. Coats on what you just said. I don't mean to dismiss the concerns about physical abuse and sexual abuse in children. I guess I was taking a somewhat optimistic attitude that because these abuses have generated a great deal of publicity that both the operators of those facilities, the parents who put their children in these facilities, regulatory officials in the State, would all become concerned enough about this that we would see better screening of applicants to work in these centers, we would see more vigilance on the part of parents, in terms of visiting some of these facilities and checking out these places, so that that brand new exposure which was never contemplated by insurers when they were providing this coverage in the past, indeed, I'm sure they just didn't think it would happen or was likely to happen, I'm hoping and optimistic that those kinds of problems can and will be dealt with, not so much from an insurance angle as from a public policy standpoint.

We simply cannot allow these sorts of abuses to take place, whether it's in the home or in child care facilities. I'm assuming that that problems going to be taken care of.

Mr. Coats. Well, it's certainly not something that can't be managed within an insurance context. You are exposed to long-term liability in a lot of different areas, and you have to do a lot of different things to provide for that contingency. One last question and just a quick answer from all of you.

Looking at the situation on a short-term basis, is a State-mandated coverage an answer or is that a solution that simply poses more problems than it solves?

Mr. Kimble. Well, it's certainly not an approach that the insurance industry favors. We don't want to be forced to do involuntarily that which, in some instances in our judgment, we don't choose to do voluntarily. Also, we find often in a joint underwriting association situation the rates are artificially reduced. And that also clearly causes some problems.

A joint underwriting association should never be viewed as the first step. That's the last step. That's the last available solution. A market assistance program approach or some sort of linking up both insureds and insurers, simply through improving sources of information should be the first approach taken in solving the availability problem.

Ms. Walters. I would share the views just expressed by Mr. Kimble. And would add only this: When dealing with commercial coverages, which is what we are talking about here, it may require a great deal more shopping around for insurance than many of us are used to doing, when we buy our homeowners coverage and when we buy our personal lines coverage. It is a little more difficult, and it takes more perseverance and I would hope that the private marketplace could solve some of these problems, and would urge those who are trying to find coverage, perservere and recognize that it is different than getting auto coverage or homeowners coverage.

Chairman Miller. The time has expired. Excuse me, you wanted to respond?

Mr. Neuhauser. The answer to the question is, no.

Chairman Miller. Congresswoman Boggs?

Mrs. Johnson. Mr. Chairman, could I just ask the gentleman to yield to me just a moment because I have to leave?

To follow up on this point, if you don't want something to be mandated, are you beginning to follow through on the kinds of suggestions, Mr. Kimble, that you made in your testimony that communication, working with the private sector, and, through that kind of effort, you hope to clarify what kinds of regulations, constraints, exclusions or whatever could be put in place that would be both comfortable for the providers and would enable you by September to provide the kinds of insurance that these people desperately need and that we can't allow them to go forward without?

Mr. Kimble. Absolutely. We are not interested in joint underwriting associations and we are going to work hard to solve the problem in order to avoid them.

Mrs. Johnson. Well, we'd like to be kept abreast of the communications that you are developing with the insurance industry and with the day care industry in your efforts to define these kinds of regulations.

Mr. **Kimble**. Certainly.

Chairman **Miller**. Thank you.

Mrs. **Johnson**. Thank you, Mr. Chairman. I appreciate it.

Chairman **Miller**. Congresswoman Boggs?

Mrs. **Boggs**. Thank you, Mr. Chairman. Thank all of you for your testimony.

Mr. Kimble, I suppose that your caution that prudence is indicated and not panic should be taken very seriously since your association has been advising the insurance industry and the rest of the country in a very reasonable fashion since 1866.

But I was especially interested in your comments that day care loss ratios are similar to all other lines of insurance coverage. And so I don't understand why day care coverage should be especially singled out with a few other categories for some increased amounts of premiums and for the panic that apparently is existing about being able to cover them.

Would you like to comment on that?

Mr. **Kimble**. Yes; not necessarily all lines, but certainly all commercial lines and in particular, the general liability lines. Unfortunately day care centers aren't being singled out. All other commercial lines are experiencing substantial rate increase and in some instances also availability problems. That would be true of professional liability, all pollution coverages, commercial auto coverages as well as day care centers. Medical malpractice, the list goes on and on.

Mrs. **Boggs**. Thank you. And Mr. Neuhauser, I notice that you felt that the primary problem is the application of the tort system, and you gave some fairly compelling examples of what might happen under that system.

And then in your suggested solutions, you said the stricter licensing and enforcement thereof, of course, was indicated. In our insurance industry, we have State commissions and State commissioners, and that's as it should be. And we have varying State laws about day care centers and the licensing thereof.

I'm sure that we will be hearing later from a member of the Connecticut Assembly who will address that in particular. But don't you think that the requirement for insurance that the States have imposed on day care centers means that there will be stricter licensing; and, therefore, if there are stricter licensing requirements, and one of those requirements is that there must be insurance coverage, that you are going to find enforcement sufficient to have the industry able to comply with the State's requirements for the operation of day care centers?

Mr. **Neuhauser**. My comments basically were directed to the licensing requirements of the child care providers. And I understand that in many States, and I don't believe it is all States, that insurance is part of that licensing requirement. But simply having the insurance policy in terms of the licensing is only a small piece when I referred to stricter licensing requirements.

The child staff ratios, whether those child staff ratios should vary for instance for toddlers or for older children; the actual construction of the building, whether it is intended for child care use;

the qualifications of the staff director; the availability of first aid, would also fall into those licensing requirements that could make a child care provider a far more or far less dangerous risk to the insurance industry.

And of course the enforcement, as we are all aware, particularly in insurance, the enforcement of insurance requlations varies substantially State to State. The enforcement of insurance regulation for example in Texas is extremely stringent. The enforcement of rules in the State of California is stringent, although they have no rules as respects filing.

Again, those items would vary. The simple requirement to have an insurance policy I don't believe that solves the licensing problem that I was referring to when I talked about stricter licensing.

Mrs. Boggs. Thank you very much. Thank you, Mr. Chairman.

Chairman Miller. Congressman Wolf?

Mr. Wolf. I think it is important, as Ms. Johnson was saying, that the industry respond as quickly as possible because otherwise there will be an outcry. I've heard from my congressional district already. Soon I think we're going to begin to find a lot of parents getting letters from the day care providers as they pick their children up saying contact your Congressman, contact your Senator, or contact your State legislator or insurance commissioner asking them to do something about this insurance problem.

And it's going to be a growing thing. You can see it beginning. I just sense the concern about the issue is beginning to grow and grow. I think it is important that you respond as quickly as possible.

The insurance commissioner from Maryland seemed to say that he thought it was a temporary crisis. And he seemed to feel that in a year or two that it would be pretty much resolved. Do you all agree with that? Do you believe it's a temporary crisis; and, if so, how long of a temporary crisis do you think it is?

Ms. Walters. Let me start and give the other two something to shoot at. I think I would agree with Commissioner Muhl that for this particular class of business, as I said earlier, I don't see this as having the same catastrophic potential as some of the other exposures that I described, so I would hope that this would be manageable by in large and could be dealt with.

Let's make sure we know what we're talking about though. All morning, I think we've been muddling a lot of problems. We've been muddling the problem of cancellations and we've been talking about availability at any price, and then we sort of talked around affordability questions.

We would be doing everyone a disservice if we tried to leave the impression that premiums are not going to go up in this line of insurance. Rates are going to have to go up. They must be sufficient to cover loss costs. So I think, given that understanding, I believe that this is a manageable problem. Long term, however, I do disagree with Commissioner Muhl, when he said he was hopeful that the capacity problems and the capacity shortage would be behind us perhaps by the end of next year. I don't share that view.

I'm afraid the capacity shortage and the attendant marketplace problems are going to be with us as a society for a couple years beyond that.

Mr. **Wolf**. So you see it as really a long-term problem?

Ms. **Walters**. Not particularly for this class, necessarily, but a general availability problems and affordability problems, are going to be with us for selective commercial classes. I'm afraid, for the next couple of years.

Mr. **Wolf**. Do either of you want to comment?

Mr. **Kimble**. Recognizing that we are in the realm of speculation, the premium volume and the loss ratio and the amount of exposure suggested in the Insurance Services Offices' data, indicate that given that we can charge a proper premium, we should be able to respond in this area. This particular line of coverage doesn't appear to offer catastrophic loss potential. Those are the lines which we have to be very, very prudent about, given our drain on surplus and our capacity shortfall.

This particular line doesn't appear to have catastrophic exposure associated with it, so if we can charge a proper premium, those companies which have moved out of the market, should, given some reasonable period of time, be replaced by other companies moving into the market.

Mr. **Neuhauser**. Basically, I believe there will be a long-term problem for child care providers. I have to take exception, particularly because of the potential implications of child abuse, physical abuse, et cetera. There are certain other problems that are inherent here as well. The absence premium size for a child care provider is extremely low. So when we talk about doubling or tripling or quadrupling a premium to $3,000 or $4,000, with the exposure of $300,000 or $1 million to a single case some years in the future, a situation that we all know exists, When I say "we all know exists" we know that child abuse exists, considering our tort system and the movement in the judgments that have been made, there is the potential for catastrophies 10, 15, 20 years down the road in this class, to the same extent that there is the potential for catastrophies from a drug manufacturer or a chemical manufacturer. There is a latent exposure that is unknown.

And the interpretation of that or the expectation of that against a very small gain today may provide a problem for a very long period of time for child care providers.

Mr. **Wolf**. Do you see this happening even if the rates are dramatically increased?

Mr. **Neuhauser**. Yes, sir, because I don't believe that one is—I think we've established pretty well that we can't determine what the value, the dollar value is going to be on this specific problem to this industry. We do not know, we do not know when it is going to have to be paid, when the judgments are going to start coming, if in fact they are. So there's a huge unknown rise. And the insurance industry here—similarly to pollution I should point out; pollution is another similar kind of situation—we don't know what we're going to be looking at as an insurance industry 5, 10, 15 years down the road. And basically I think the problem with insurance for child care providers today is part of the overall problem with a tort system whereby the numbers that the insurance industry puts out today may be spent as a result of an interpretation that comes 10, 15, or 20 years from today.

Mr. Kimble. Mr. Wolf, what's being discussed now is characterized as the long-tail phenomenon. There is a belief that because you're dealing with children, and the statute of limitation doesn't run until the child reaches the age of majority, that some of these cases could be hidden. You couple that possibility with the adverse publicity and perhaps some of these children or parents who have been quiet about sexual or physical abuse because of their concern about their own child, those cases may be filed in large numbers over a short period of time.

That's the long latency here. It is a real possibility.

Mr. Wolf. Thank you. No further questions.

Chairman Miller. Thank you. Mr. Rowland?

Mr. Rowland. Thank you, Mr. Chairman. It appears that the unavailability of liability insurance is multifaceted and the cause of that is multifaceted, we thought about the perception and cannot substantiate actuarily any reason for child care centers not being able to get the insurance at this time. But you just mentioned the long tail problem as one of the reasons.

But Ms. Walters, in looking at your statement here, you said insurers must develop solid business products and their prices must correctly reflect the cost and expenses of coverage provided and significant premium increases are needed. And you also said a major contributing factor to these major miserable underwriting losses and the tightening insurance market are the excessive costs of the civil justice system.

And Mr. Neuhauser, you said that the primary problem clearly appears to be the application of our tort system, and you said any permanent solution would require significant changes in our tort system. Can you give me some idea about the relative contribution that the poor investments that have been made by insurance companies and the lack of return on their investments decrease in their reserve is compared to what the contribution by the tort system is making to the problem that we have?

Ms. Walters. If I might respond to that, Mr. Rowland. I read a statement like that somewhere else, I think, in some testimony that was given at the previous hearing. Insurance companies haven't made poor investments; they made record amounts of investment income; that's not been the problem. And that's why this cycle—you'll hear that the insurance industry is a cyclical industry and you may hear some more of that—this cycle is unlike any the insurance industry has ever gone through since—well, in the history of the insurance business. It's not poor investment practices or investment losses that have created a $2 billion decline in surplus and a $3.8 billion negative cash flow.

It's not the investments. They've done very well on the investments, but they haven't done well enough to overcome $21.3 billion in undercharges that have resulted in underwriting losses, so it's not the investment income side; it's been the operations of the insurance function, if you will. And as I say, this is different from any previous cycle so, in a sense, we can't take any comfort in the fact, well, we've had other cycles before and we've gotten out of them and surely this is going to happen again.

We cannot because this is so different. There have been other times in the insurance industry when, as an industry, surplus declined and declined somewhat significantly, but never before has the surplus decline come about because of operating losses. It has previously come about because of stock market declines, which generally effect the whole economy and of course, as the stock market goes down and depletes surplus and net worth for other companies, as well, when the stock market turns around and starts rising again, surplus increases and in a sense it takes care of itself.

This isn't the problem here. We had in 1984 basically a flat stock market and there were modest capital gains. This surplus decline was caused by inadequacy of pricing; that's it. Inadequacy of pricing that went on for about 4 or 5 or 6 years. The industry has finally realized that. They are the masters of their own fate to some extent.

When you've charged inadequate prices for years, it takes a long time to turn those prices around and get them to be back where they should be today. There is no way to recoup those underwriting losses. It's not going to happen, but you do have to bring those prices up to where they should be.

Chairman **Miller**. How are inadequate prices determined? Again, we are told by the insurance commissioner that they, in theory, at least in the State of Maryland, are not supposed to allow insurance companies to charge premiums that do not provide for adequate coverage. Yet, we're told we have a history here of inadequate pricing. Were those inadequate prices intentional, to gain market share?

Ms. **Walters**. The, the competitive factors which lowered the price in the marketplace, yes, was to gain market share.

Chairman **Miller**. But you're not supposed to be able to do that?

Ms. **Walters**. But with the thought that on a net basis, there would be positive operating incomes. No company and no business tries to operate at a loss, and these companies did not, either.

Chairman **Miller**. Let's understand though, that there are some business judgments which have proven to be brilliant, to take a calculated loss, in return for a long term profit. Some people suggest that that's why we don't do well against the Japanese in electronics; because they're willing to take short term losses for long term gains.

My concern is we're told on one hand that the regulation says the industry is not allowed to charge premiums which fail to provide for adequate coverage of their losses, and yet we're told historically that is what has been done. We're also told, in effect, that the industry in many lines of coverage engaged in this as a competitive tool.

I think there's an internal inconsistency between those two statements. What you term good competition some people might term illegal.

Ms. **Walters**. I didn't term it good competition. I think I made it very clear that I was not making a quality judgment.

Chairman **Miller**. No, but the facts speak for themselves.

Ms. **Walters**. Let me see if I can't clear that up for you. It's true. Every rating law in the United States says rates shall not be excessive, inadequate or unfairly discriminatory. It is also true that ratemaking is part art and part science, and there is a great deal of judgment that goes on.

Chairman **Miller**. As soon as I separate the art from the science, I'll be a happy man.

Ms. **Walters**. Oh, wouldn't we all. But the fact is when you're trying to make decisions today about the price you must charge today when the true costs are not going to be known for some instances several years down the pike, you really are not going to know those costs. But you're trying to set the price so that you do, overall, make a profit.

And companies have been doing that; they have not been deliberately writing this business knowing overall they were going to lose money. Obviously, they thought they were going to be able to continue to make money.

Mr. **Rowland**. If I may reclaim my time for a moment?

Chairman **Miller**. Sure.

Mr. **Rowland**. And interject right at that point. They thought they were going to make a profit. Now, I'm trying to get to the reason as to why they didn't make a profit and I'd like to hear your comment on how our present tort system is administered in that respect?

Ms. **Walters**. Because, in my opinion as an observer of the scene, there were a couple of things that were going on at the same time. First, we are describing in more detailed terms, cash flow underwriting, as Mr. Muhl referred to it. Companies writing the business at a certain price a price which they knew was going to be inadequate to cover the losses, but they also reflect investment income, mostly on a judgmental basis, I'm roughly going to say, and assuming that they could make up for it, knowing what they knew about the risks they were insuring and the class of business they were insuring, they were estimating, I can write this business at this price.

I know the price, the premium isn't going to be sufficient to cover the losses and expenses, but I'm going, I believe that the amount of money that I make on investment income, by having that cash flow to invest, will be sufficient to allow me to make an operating profit.

While they were doing that and while the companies were competing with each other to expand their business, at the same time, the courts, and juries and legislatures were making decisions about the products that were already in the marketplace; about those policies that had already been written under one set of assumptions. Assuming a relatively stable base of losses or a projection of what the loss experience was going to be, under a certain set of rules. After the business is on the books, the rules changed.

Because of court interpretations, again, perhaps higher claims than were ever anticipated; changes in the rules after those policies were put in the books, that have caused those losses to be a lot higher than originally anticipated.

Let me give you one specific example. Commercial general liability policies have for the last I guess 8, 10, 12 years been written with a pollution exclusion—this is not in this area but it gives you an example—that said, these losses will not be paid unless they are sudden and accidental.

And we have had courts all over the land effectively doing away with the sudden and accidental exclusion and finding coverage when in fact the coverage was slow, it was not accidental, certainly wasn't intentional, but they've just redefined the whole terms of the contract, and this is what has been taking place during this period of competition.

Mr. **Rowland**. So then you would say that our present tort system, as it is applied, has a great deal to do with the difficulty that we find ourselves insofar as the availability of liability insurance is concerned?

Ms. **Walters**. I believe it does, add I believe what compounds the problem—maybe now we can look at what happened in the past, and say Ok, we can explain it. But the next question is, how do you deal with it? And I think the changes in the rules, if you will, have led many insurers—indeed Lloyds of London—to say, we don't know what the rules are now. We have no confidence anymore that the rules of the game as they exist today will continue to be the rules of the game tomorrow or the next year, or the year after that.

In fact, Peter Miller who is the chairman of the Board of Lloyds, has stated in a series of public speeches that he made around this country in the last 6 or 8 weeks, that Lloyds of London has walked away from the U.S. casualty business. He said, we can't deal with your civil justice system; we will not insure your commercial contracts because we just can't deal with it; we don't know what the rules are.

Mr. **Rowland**. Mr. Chairman, I'm not going to ask any more questions, but I would like to hear Mr. Neuhauser respond, also.

Mr. **Neuhauser**. Ms. Walters covered most of the areas. One point though, sir, as respects the investments that an insurance company makes. Everyone of those investments, every individual investment is itemized in the schedules that are presented to each of the State insurance commissioners. So all of the bond holding, stock holdings, et cetera, are enumerated for public consumption. And for the most part, and in most States they are very strictly regulated.

As respects the tort system, I think the example of the elimination of the sudden and accidental exclusion, where courts have said that gradual pollution over 10 years was as a result of something that was sudden and accidental that may have happened during that period, that interpretation has been taken particularly again with asbestos. And when we're talking about long-term coverage, I don't believe that there are actuaries that can predict what the implications are of exposure if the rules change.

And the rules have been changing as it respects jury verdicts very quickly. The insurance industry has been very much affected by that, as a result of providing coverage that comes into play in numerous circumstances where it was never intended to cover. And again, the problem as we see it with the child care provider's insurance is part of a broader area, and this problem can extend to other areas, if there's an anticipation of something that can go wrong today or in the future that might be affected by a changing civil justice system.

Mr. **Kimble**. If I could generalize just for 1 minute. Until the very early 1970's, most of our insurance policies were designed to respond to accidents. Something which was traumatic. In the last

15 years or so, there's been a movement toward nontraumatic situations—multiple causation, long latency diseases. What we're finding is that either through innovative new tort concepts or through courtroom misinterpretations, we're responding and paying claims for those multiple causation long latency diseases when in many cases we never intended to provide coverage.

Certainly, we're affected by the tort system. Our policies are designed to service those tort liability concepts so, yes, we're very much affected by them. What we've been grappling with for the last decade or so is a way to design our contracts in a fashion so that they respond to what we intend them to respond to.

That's reasonably easy to do when you are dealing with accidents—a traumatic injury, a fender bender, fingers in a punch press. However, when you're talking about nontraumatic situations, multiple causation long latency diseases, those words of art in the insurance contract simply don't work as well.

Chairman MILLER. Congressman Wheat?

Mr. WHEAT. Thank you, Mr. Chairman. I am not going to take too long to question. Let me first say to the panel, I appreciate your excellent testimony, and certainly understand the complexity of the cause of the problems better than I did before the testimony. But I am still curious about the separation of the two problems at which we are looking. One problem, of course, is that of higher cost, and the other is the lack of availability of insurance. I am not sure that the proposed solutions actually deal with both of these problems. As I understand it, you are suggesting such things as better communication between the day care industry and the insurance industry. But in fact, even with better communication, all you are going to tell day care providers is that they have to pay more money for insurance.

Is that basically it?

Mr. KIMBLE. It's clear that premiums are going to increase. That's necessary, responsible and prudent, from our point of view. What we hope to be able to do is to locate insurers for these day care center owner/operators who are interested in providing the coverage. That would be the principal service.

Mr. WHEAT. Additionally, though, you wanted to work not only with the day care centers, but also with States and regulatory agencies to try and make sure that all reasonable precautions can be taken so that day care centers can operate with the highest possible standards of efficiency and safety.

As the system is currently structured, losses from day care centers are not out of line with other kinds of insurance. Yet we already see the lack of availability of insurance due to either the short-term or long-term factors you discuss. I am not sure how you can reconcile talk about these long-term factors and, at the same time, make statements that insuring day care centers does not have the same potential for catastrophic loss as does insuring for medical malpractice, for instance.

What you are saying is that it does not really matter how competent centers are in providing day care in the safest, most efficient way possible. There will still be this panic, or fear—whether it is reasonable or not—about the possibility of catastrophic long-term losses, and we will still have an availability problem.

Mr. **Kimble**. I would agree with you when you suggest the losses for day care centers are not out of line. The losses, however, are substantial. Unfortunately, they are substantial as well in all of those other lines.

Mr. **Wheat**. But in some of the other lines, if you raise the prices enough, you will be able to cover the losses, and continue to provide insurance and make a reasonable profit. You are not suggesting that you can do that with day care. You are suggesting that the same factors you are afraid of in the long term, will still provide disincentives to insurance companies writing insurance for day care centers.

Mr. **Walters**. Mr. Wheat, we're suggesting that the problems in commercial general liability are all over the place. There's disagreement among the three of us as to the magnitude of the problem for this particular class.

I would again emphasize that this class of business is not alone in facing problems. In fact, I would say without danger I'm sure of my colleagues contradicting me, that there are other areas and other classes of commercial general liability business where the problems are so immense there is no market, period. There are no insurers providing coverage for certain types of risks and none are going to be providing in the foreseeable future, and EPA can pass all the regulations they like, and State laws can be enacted, but if the insurance isn't available, it isn't available and won't be available.

And that is the condition today for a lot of commercial general liability business. And rates are going up drammatically. But I would most emphatically disagree with you that there are quite a few classes of business where insurance will not be provided at any price.

Mr. **Wheat**. To point out there are other industries that also share the problem and perhaps some to an even greater degree than the day care industry, really does not do a great deal of good to solve the day care industry's problem.

Ms. **Walters**. Sure. I understand that. I understand that.

Mr. **Wheat**. Are you suggesting that day care is moving toward that category of industry where there will be no insurance available?

Ms. **Walters**. No; I think the discussion among the three of us earlier made it very clear that we see even among the three of us, see this problem a little differently. I cannot disagree totally with the analysis presented by Mr. Neuhauser. He may be right, and I'm sure some underwriters do see a potential here in this class, which is not unlike the potential problems they see for nurse midwives and obstetricians. Because you are dealing with young children.

I see his point. On the other hand, my perspective is this, you're dealing with young children here, but by in large I'm not sure it's the same catastrophic potential as you are dealing with in child birth, for example. I suggest the marketplace, the insurance marketplace probably reflects the same differences of opinion as we have expressed to you today. This follows through with the theme that Mr. Kimble tried to explain earlier, that we have had, as we understand from reading the literature, many cancellations of some policies.

We've had major providers, companies who have provided a market for this type of insurance, for whatever their reasons, have decided they're going to get out of it. So they are leaving. They are familiar with the business. They've got their own problems; they've got to get out of it. Now, that's leaving a whole host of these child care providers without any place to go. So, it's sort of a very quick turnaround that we're looking at here and not all companies who write commercial lines write every single commercial line, so it's going to take a while for the educational process and the judgments of the individual companies with their different capacity problems or capacity availability to come to grips with this marketplace.

I think Mr. Kimble and I are a little more optimistic that as the educational process evolves, as we see better licensing standards of providers, that the insurance marketplace on a voluntary basis will be more apt, we believe, to deal with this. Mr. Neuhauser sees it as a more catastrophic problem and I think some underwriters will see it that way, but there are literally hundreds if not thousands of insurance companies out there, and I think that there will be differences of opinion in there, and I'm hoping most of the providers can be taken care of.

Mr. NEUHAUSER. I would like to point out that I see it as potentially a more catastrophic problem; I do not necessarily see it as a more catastrophic problem. We've done a lot of research, and I'm parodying to some extent the words of people that I've spoken to.

By the way, I would like to point out that I do believe there are some short-term fixes, and I did present some of that in my testimony toward the end, with references to exclusions for physical and sexual abuse, if we can get around the situation that Mr. Kimble talked about. Potentially structuring limits of liability or defining what types of what award is going to be paid.

Mr. WHEAT. Mr. Neuhauser, let me interject and ask you whether you really see those as short-term fixes, when the real fear of insurance companies seems to be the long-term losses they might be subject to, based on future court interpretations of contracts being written now. While trying to limit the losses from current contracts, you have no idea what direction the courts will be going in the future. Would you really consider such exclusions any kind of assurance that those catastrophic losses will not occur?

Mr. NEUHAUSER. No, I do not consider that any kind of assurance that those catastrophic losses would not occur.

Mr. WHEAT. In which case, there would be almost as great a degree of uncertainty about the future possibility of catastrophic losses as there is now. Really, it does not suggest any real solution to the short-term problem of lack of availability of insurance.

I just want to find out what you really see as an incentive to insurance companies to provide insurance under the best of scenarios. The problem will take care of itself over a few years, but what about right now?

You know, the problem is getting worse every day.

Mr. KIMBLE. An insurance solution to this problem is a necessity, because we need day care centers. The commissioner from Maryland earlier referenced joint underwriting associations. That's an involuntary, artificial insurance mechanism. California, I know, introduced a JUA bill just the other day.

That is something which we don't appreciate very much. We're not interested in involuntary insurance mechanisms. That's leverage which will——

Mr. **Wheat**. Are you going to wait until the States pass laws requiring mandatory insurance coverage for day care centers?

Mr. **Kimble**. My work is at the Federal level, and there are several Federal laws which contain what are called financial responsibility requirements, they are in the Resource Conservation Recovery Act. The Motor Carrier Act, and Superfund, I opposed each one of those financial responsibility requirements, unsuccessfully, but I opposed them. Principally because we believe if you mandate insurance as a prerequisite for doing business, what naturally follows is some sort of artificial insurance mechanism which we must participate in.

So, yes, we have opposed those. In any case, the potential for JUA's will create leverage which will energize the insurance industry and we'll do everything we can to provide it on a voluntary basis. It's speculation at this point, as to whether we'll be able to.

Mr. **Wheat**. What you are suggesting, then, for those of us who are on this panel, is that the more seriously we look at JUA's as an alternative, the more seriously and energetically you think the insurance industry will try, by itself, to come up with some real alternatives?

Mr. **Kimble**. If you'd made that statement 1 month ago, I would have agreed with you. But you are a little late. It's already happening.

Mr. **Wheat**. Thank you very much, Mr. Chairman.

Chairman **Miller**. To follow up on that point for a moment. In my discussions with people on the Ways and Means Committee, who are going to pay very large insurance premiums, through the Head Start and title XX Daycare Programs, it is clear that discussion is going on right now. We don't have the jurisdiction in this committee. But for those committees that fund these programs, they're going to have more and more of moneys that were dedicated to services, going to insurance premiums. There's a very substantial amount of concern there.

I don't know whether the States are going to work out their joint underwriting agreements, or not. But it's very clear, I think, and this point has been driven home by Mr. Wheat, that we may be in a transition period, but 1 year without coverage or 6 months without coverage, will destroy a number of providers of child care. They simply cannot provide a service with those insurance costs. We will lose those slots for children of working parents and others.

And so, to suggest that there's going to be a hiatus here for 1 year or 6 months or for whatever period of time, while the insurance industry rearranges itself, I just think is unacceptable in terms of public policy.

You are asking responsible people to take an irresponsible course of action for a period of time.

Mr. **Kimble**. We're hoping that, given 1 month, that there will be enough progress so that the trend is clear and we can all relax a little bit in terms of the potential availability problem. But I would think within a month a trend will appear one way or the other.

Chairman **Miller**. We've got a trend going now, and we hope you can reverse it. Mr. Weiss?

Mr. **Weiss**. Thank you, Mr. Chairman. As I understand your testimony, you're really saying that your actions within the day care area have to do with your pessimistic view of the performance of the insurance industry over all, not just in day care or any other specific field. You refer to this as an unprecedented cyclical downturn.

But I gather that this pessimism is not shared by people who invest in insurance industry stock. In fact, the levels and ranges of prices on Wall Street are demonstrating a great deal of optimism in the insurance industry.

If that's an accurate presentation of the situation, how do you account for this apparent contradiction?

Ms. **Walters**. Oh, I don't see any contradiction at all, Mr. Weiss. In fact, historically, if you follow the insurance industry and investment policies and practices on the stock market, I think it's been abundantly clear that over the years, first of all the primary investors in insurance companies are institutions, institutional investors hold most of the insurance company stocks.

They are relatively sophisticated investors; those investors rely on the same series of analyses of brokerage houses and investment houses who have strong reputations for following insurance company stocks, and it's well known and well documented that the institutional investors try to buy in and indeed do buy into insurance company stocks at the bottom of a cycle. And it's fairly easy to see once the cycle has turned and the signs start appearing that prices are firming and that the downward trend is indeed in the process of reversing itself and well-documented. People have seen it.

We saw the signs beginning at the end of 1984, last part of 1984 and certainly in the first quarter of 1985. The institutions respond to this by saying this is the time to get into the insurance business because we're going to now start to ride the crest as the wave gets better in the ensuing years so that's what's started to happen most recently.

I might add that 1984, you know, I've cited figures before I think another most frightening figure is that the top 100 insurer groups in the United States, over 50 percent, over half the top 100 companies in the United States had a negative return on net worth. Clearly, that was pretty dismal, definitely at the bottom. Things have started to turn and things are looking a little better.

Indeed, to some extent, the dire capacity shortage that we saw immediately for 1985 may be abating somewhat for the early part of this year because many stock insurers have gone to the capital market, successfully, and for the same reason that I described about institutional investors now wanting to buy in on insurance stocks, because they will start to improve.

Mr. **Weiss**. But obviously they wouldn't be getting into it if they anticipated an unmitigated disaster. They see things moving positively.

Ms. WALTERS. Of course, so do we all. So do we all. That's why we were describing here. We described what has happened to have led us to the current situation.

Mr. WEISS. Ok. If that's the case, then why get out of these fields when the controlling factor is no longer continued disaster but in fact significant improvement?

Ms. WALTERS. Because, as a result of what took place over the last 6, 7, and 8 years, there has been a diminution of surplus. The surplus of the industry declined by $2 billion in 1984. An insurance company cannot just go out and write all the business it wants. As Commissioner Muhl described earlier, there is a limitation based on financially how secure each and every company is. There's a limitation on how much business it can write; it just can't write all the business out there.

That limitation is defined by the amount of policyholder surplus that that company has, and the industry, as a whole, has a reduced surplus, and it can only write so much business.

That is what's in this capacity shortage study which I described and I'm going to leave with the committee. Because of that, very simple numbers, an analysis of the ratio of premiums to net worth that companies may maintain, how are they going to make contributions to surplus so that surplus can grow.

As a result of a whole complex series of relatively conservative estimates, we are seeing that even though things are starting to improve, there will be a capacity shortage for years.

Mr. WEISS. But then all the discussions about the potential problems in the day care area really have nothing to do with this. Decisions are made according to the amount of money you've got available. You're then making judgments as to where you want to put your money because you're limited in the amount of money that's available. But, given the description that you've made of the optimistic future of the industry, and the lack of demonstrated problems in day care, it's sort of an arbitrary, panicky judgment not based on reality.

Ms. WALTERS. No; I don't share that view at all. As we described several times earlier today, the premium inadequacies are shared by all commercial lines. Premiums have got to keep in line with loss costs. Those premiums are going to go up; there's no two ways about it. You can't keep losing $2 billion a year on an industry wide basis in surplus and continue to survive.

And the American economy can't survive without a viable insurance industry.

Mr. WEISS. Yes, but you're not talking just about premium increases. You're talking about cancellation.

Ms. WALTERS. No, sir, in fact, very much earlier I, if you'll recall, I said, this whole description's getting very muddled because it's not clear are we talking about in some instances cancellations, in other instances we're talking about increases in rates, affordability problems, in other instances, we're talking about availability problems, and I think it's fair to say that all of those problems, to some extent, effect the day care industry. In different states, in different jurisdictions, for various and sundry reasons.

Some of the problems are easier to deal with than others, and I think all we were trying to do was put this class and this problem in context of the larger problem. Some of us don't see it as being as great as some others, but there will be some underwriters who do share the view as expressed by Mr. Neuhauser, that this has the potential that I as an underwriter or a manager of this insurance company, looking at my financial condition, is a risk I cannot afford to put on the books of my company.

But they'll be another underwriter that says, we're financially sound; we've got pretty good capacity. We're evaluating this particular risk and we think we can handle it.

Mr. WEISS. Thank you. Thank you, Mr. Chairman.

Chairman MILLER. Thank you very much for your testimony and assistance.

The next panel will be made up of the Honorable Peter Nystrom, who's a representative, General Assembly of the State of Connecticut; Mr. Robert Hunter, who is the president of National Insurance Consumer Organization; and Tom Birch, who is the legislative counsel for the National Child Abuse Coalition.

Mr. Nystrom, we'll hear from you first, and your statement will be put into the record, and the extent to which you want to summarize it will be appreciated.

Mr. NYSTROM. Thank you, Mr. Chairman.

STATEMENT OF HON. PETER NYSTROM, REPRESENTATIVE, GENERAL ASSEMBLY, CONNECTICUT

Mr. NYSTROM. I want to thank the committee for the opportunity to speak to you today. Before I begin, I would like to introduce Mrs. Jeannie Millstein who's a member of the Permanent Commission on the Status of Women who accompanied me today from Connecticut. She's also the chairman of the Child Day Care Council which has a leading role in child day care advocacy in the State of Connecticut.

My testimony has been submitted for the record, so I'm going to highlight what I feel are some of the areas that we have been looking at in the State of Connecticut. As a member of the Human Services Committee, I have been asked to take a lead role in this particular issue. Over the last 5 weeks we have held some meetings with the insurance commissioners office and members of the insurance industry. We have had some public hearings with members of different departments that have a cognizance in the area of day care in the State of Connecticut, and also we had a public hearing last night with providers of day care. From this we have seen problems occurring due to cancellation of policies, increase in premiums.

We had one individual last night whose original policy was $280. It went up 1,000 percent, $2,800. For one day care center, that's quite a cost to absorb. In fact, the premium was up front and not rated out over a year basis. I will highlight for you some of the ideas that we have come up with in the State of Connecticut, and they are just ideas at this point.

It would be one idea that the State of Connecticut insures itself in the area of child abuse, and that would then allow the insurance companies to write policies for day care coverage liability insurance, excluding the child abuse area. The reason for that is basically that we want the day care centers, group homes, and family day care homes to remain open. We need more day care in the State of Connecticut; we do not need less.

If they do not have insurance, we are going to have less. And if that occurs, then we're going to see an increase in our welfare rolls, because there are a lot of single parents who need day care in order for them to maintain their jobs. If they do not have the day care service, they're going to have to go back on the welfare because it will be more financially sound to do so.

Some of the things I've heard this morning and early this afternoon I wish not to repeat. The insurance industry's loss I think has been due basically to what has been stated today. However, putting it on the backs of day care, I feel is not necessary. There has been a lot of potential risk that I think is being used as a reason for the increase in premiums, the reduction of coverage, the adding of deductibles, and the overall cancellation of policies.

I think it is somewhat of a hysteria that is out there. I do not believe it is based on sound data because what we have been told in Connecticut, and I cannot speak for any other state, is that they do not have sound data for the incidents of child abuse in day care centers.

Something else that occurs is that they were not even aware, at least in the insurance commissioner's office, that there are unlicensed day care centers in the State of Connecticut, which happens to be illegal, but they are functioning. It's estimated that approximately four-fifths of the children in day care centers in the State of Connecticut are in unlicensed centers.

We're talking about a total of about 300,000 kids who would require day care presently, based on our information, and really only 20 percent of them are in licensed facilities. That is a concern of the insurance industry, and I think that's rightly so. If it's unlicensed, you don't know what you have for a center, and what's being provided in the name of service.

Something else that is also being looked at is the possibility of the day care industry self-insuring itself. However, there is a problem with that. In order to do that, at least from the information that's been made available to myself, you probably would have to have at least 200,000 kids involved as a whole group, that would be insured. Other than that, you couldn't do it financially.

So, consequently, that's a very large organization problem. Requiring insurance companies to write insurance for day care is another possibility. I'm quite sure it would not be received very well. However, I think the State of Connecticut has an obligation to children to protect them, and also to the rest of the State's populous to ensure that that we do not increase our welfare rolls, that we provide an environment that allows for job employment, and overall again, for the protection of the kids.

Chairman **Miller**. Thank you. Mr. Hunter?

[Prepared statement of Peter Nystrom follows:]

PREPARED STATEMENT OF PETER NYSTROM, REPRESENTATIVE STATE OF CONNECTICUT, GENERAL ASSEMBLY

Good morning Mr. Chairman and members of the Select Committee on Children, Youth and Families. My name is Peter Nystrom, and I am the State Representative from the 46th District of Connecticut. I am here this morning to tell you that the State of Connecticut is in the process of conducting an inquiry into the issue of insurance and day care.

In Connecticut we require that all day care providers be licensed by the state. State statute provides for a fine of up to one hundred dollars per day of any unlicensed day care provider.

The two departments who grant a license are the Department of Health Services which licenses all group day care homes (six to twelve children) and day care centers (twelve or more children with increased staffing requirements based on the total number of children) and the Department of Human Resources who's specific responsibility is for licensing and monitoring family day care homes (one to six children). The Department of Human Resources also provides a subsidy for families who are low-income for child care.

Over the last five weeks we have been conducting meetings and public hearings gathering information about the insurance issue and day care. The following information is only at best a set of recommendations for your review. Please do not consider them to be in concrete. As time goes on we will be modifying or changing them.

Along with the recommendations I have enclosed further information regarding a Liability Insurance Guide for Child Care Centers, a copy of recent law passed in Connecticut and a chart concerning liability insurance issue.

Recommendations:

1. The State of Connecticut may by statute require all insurance companies to write insurance coverage for day care providers; excluding coverage for child abuse. Such coverage would only be available to those providers who are licensed by the state. This would create an insurance pool which would spread the risk among the entire insurance industry. Thus it would be the hope that this would allow the day care providers to pay affordable rates and remain open as the need for more day care grows.

2. Insurance premiums or actuary rates must be based on correct data. Premiums for family day care homes (one to six children) providers and group day care and day care center providers should be different. Actuary rates should take into account the specific nature of the types of services that are provided in each setting. Family day care homes are not involved in the full educational, recreational and health services as must be provided by Connecticut law as the group day care and day care centers are Actuary rates also must reflect the income leves of each type of day care facility.

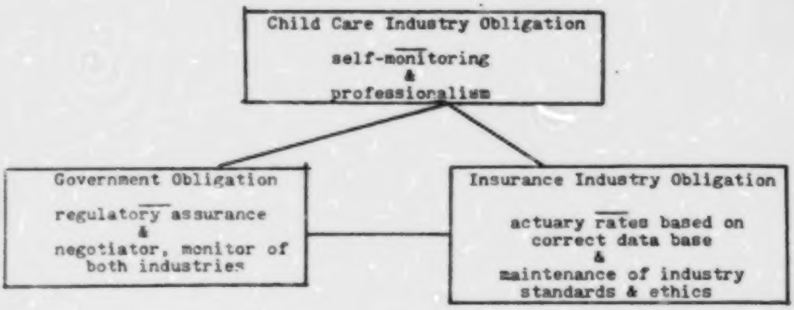
3. Provide that all home owners insurance policy application there be a section which ask the home owner if they are operating a day care. This would help to identify the understaffed system of day care. Clearly we have to devise methods of rewarding those providers who comply with the insurance industries concern of defining what day care standards are to be.

4. The State of Connecticut self insures itself to cover claims regarding child abuse. State sets up a trust fund from which any claims determined by court action will be paid. Such awards would be capped to a specific amount. Awards could be distributed by a childrens victim compensation board.

5. Child care industry self insures itself and might follow some, all or none of the procedures mentioned in recommendation no. 4.

Thank you for this opportunity to address your committee. If there are any questions I will try to answer them.

CHILD CARE LIABILITY INSURANCE ISSUE


Child Care Industry Obligation
self-monitoring
&
professionalism
Government Obligation
regulatory assurance
&
negotiator, monitor of both industries
Insurance Industry Obligation
actuary rates based on correct data base
&
maintenance of industry standards & ethics

Apparent Options:

1. Child Care Industry
   a. self-insure
   b. insist on professionalism and licensing
2. Government
   a. improve licensing standards
   b. investigate actuary rates
   c. set up emergency interim trust fund
   d. propose legislation to monitor both industries
3. Insurance Industry
   a. provide information on the data base used for rates
   b. offer insurance to ONLY
      1. licensed child care facilities & homes
      2. states where licensing is maintained
   c. re-establish a competitive market where above is available

Exchange — May 1995

①

Liability Insurance Guide for Child Care Centers

by the Child Care Law Center

You are preparing lunch for the children in your program and you accidentally spill boiling water on a child standing near the stove. The child's hands are badly burned.

Child care centers constantly face situations where there is exposure to civil liability. It is therefore important for you to take preventative measures to shield yourself and your program from possible liability. Maintaining a good safety program, following applicable licensing requirements, and purchasing insurance for your program are important preventative measures that should be taken to protect yourself and your program.

This article will discuss liability insurance for child care centers: how it works, what types of coverages are available, and how to decide what coverage is necessary for your program. Some states have laws which require child care centers to carry liability insurance in specific forms and amounts. It is important to find out if your particular state has such a law in effect.

General Liability Insurance

Child care workers have the duty to act with reasonable care while supervising and caring for the children in their custody. If a child is injured while in your program, the parents might sue the center if they think the injury was the result of the negligence of you or center staff. Negligence is a legal term that means a person was under legal duty to act with reasonable care and did not act with such care. If you have general liability insurance, the insurance company will defend you if you are sued, and, if you are found responsible, pay the money judgment up to the limits of the policy.

There are many types of liability insurance policies available.

The Child Care Law Center is a non-profit organization dedicated to upgrading information available on legal issues in the child care field. For more information, contact CCLC, 625 Market Street, Suite 815, San Francisco, CA 94105.

Comprehensive general liability insurance is the most complete form of liability insurance because it provides coverage not only for negligence which happens at the child care center, but also for negligence which occurs away from the child care center, such as on a walk, a field trip, or while the children are playing at the local playground.

A liability insurance policy will cover claims when the insurance company is reasonably convinced that you were negligent. Most general liability policies cover four types of costs

- bodily injury, which includes physical injury, pain and suffering, sickness and death;
- damage to another's property, including both destruction and loss of use;
- immediate medical relief at the time of the accident;
- the legal cost of defending the center in a lawsuit if the injured party decides to sue (the insurance company will pay for your defense even if the suit is groundless or fraudulent).

Liability Insurance Limits

Although it is clear that a comprehensive general liability policy with the appropriate endorsements can protect a child care center in many situations in which liability may arise, there are certain situations which are not covered by a general liability insurance policy, and separate coverage is required.

- **Accidents where no one is at fault.** A child in your care trips and falls while climbing out of the sandbox and injures his arm. A general liability policy will provide coverage only if the insurer believes that the injury or property damage was due to your negligence. Thus, if a child, as in the above example, is injured while in your care through no fault of the center staff, the injured party will not automatically be paid by your liability policy.

For this reason, and because many injuries to children are not anyone's fault, an accident insurance policy is worthwhile to consider. An accident insurance policy generally covers medical expenses for any injury caused by a covered accident which occurs at the child care center or while on a field trip. Most accident insurance policies list types of accidents which would be covered by the policy. For instance, most accident policies do not cover an intentional or self-inflicted injury. Thus, it is important to read the coverage and exclusions of an accident policy carefully.

- **Transporting children.** General liability policies do not cover an injury which occurs while a child is riding in a car. If your program transports children by car, such as on field trips, adequate insurance coverage is essential. (See **Transportation Insurance** below.)
- **Physical or sexual abuse.** You cannot purchase insurance to cover the intentionally wrongful or criminal acts of you or your employees. Thus, general liability insurance will not provide coverage liability for damages resulting from physical or sexual abuse to a child in your care. (See Q and A box below.)
- **Damage to your property.** General liability insurance does not cover damage to your property, whether it is owned, rented, or leased. Property insurance is written on a separate policy.

Other Liability Insurance

In addition to comprehensive general liability, there are many other forms of liability insurance which may be useful, depending on your particular needs.

- **Personal injury.** While a general liability policy covers claims relating to bodily injury and property damage, personal injury liability coverage provides protection for a libel, slander, or an invasion of privacy lawsuit, where injury is to a person's feelings or reputation. In a child care setting, this kind of claim may arise if a child care worker is involved in a disputed child custody case or reports suspected child abuse (in some states, however, child care workers are legally required to report suspected child abuse, and immune from civil or criminal liability if such a report is made). Personal injury cases brought against you by employees or former employees are not covered under standard general liability policies, but can be included for an additional fee.
- **Products liability.** The tuna which was served to the children for lunch had been inadvertently left out overnight, and one of the children gets sick as a result of eating the sandwich. Products liability insurance will protect you if you serve food or have fundraising activities, such as bake sales, and someone is injured by the food. The premium for coverage of a bake sale is usually based on gross receipts, and if there are no sales, a minimum premium is charged.
- **Owners' and tenants' liability coverage.** This is a very limited type of coverage which will cover any claims which arise from the child care operation on the premises listed on the policy. This type of policy would be useful only if your activities are specifically confined to the premises listed on the policy, i.e. you could use this coverage only if you never leave the premises with the children. The premium would most likely be based on the number of children in the child care program.
- **Contractual liability.** Almost all general liability policies exclude coverage for liability assumed under a written or oral contract. Thus, if a child care center enters into a contract with a funding source, and the contract includes a provision where the center assumes the legal liability of the other party for any damages that may arise under the contract, it would be advisable to purchase contractual liability coverage. Similarly, if a landlord inserts a hold harmless clause in a written lease agreement (where you agree not to sue the landlord if an injury occurs on the premises), since the lease is a contract, a contractual liability policy should be purchased to cover the

liability which you assumed under the lease.

Contractual liability insurance can be purchased either on a specific contract basis or on a blanket basis, which would cover all contracts made by the child care center where liability was assumed. A specific contract policy is cheaper and probably more suited to the needs of a child care center.

- **Fire legal liability.** A general liability policy will not pay for damage to anything that is in your care, custody, or control, and, therefore, would not pay for any damage which occurs to the portion of the building which you occupy. Therefore, if you rent or lease the building in which you operate your child care center, it is advisable to purchase some form of fire liability insurance. Although your landlord may have fire insurance, if you cause a fire on the premises, your landlord's insurance company will pay your landlord's claim and then attempt to collect the cost of repair to the building from you. Fire liability insurance will pay for damage sustained to the actual building if the fire was the result of your negligence.

The amount of a fire legal liability policy should be enough to completely restore the portion of the building that you are occupying in the event of a total loss. The premium is generally lower than what the building owners would pay.

- **Employee liability.** A child care center employee supervising children outside fails to notice that a toddler has wandered out of the yard. The toddler is badly scratched by a cat in a neighbor's yard and the employee is sued for negligence. Comprehensive general liability policies do not generally protect child care center employees if they are sued individually for negligence. Employees, however, can be added as additional insureds on the general liability policy. The insurance will cover employees only while they are acting within the scope of their duties for the child care center.

- **Directors' and officers' liability.** If a child care center is organized as a profit or non-profit corporation, the directors and the officers of the corporation can be individually sued. A general liability policy will protect board members and officers where the *corporation* is charged with negligence of the employees, but not if the board member or officers are separately sued for failing to make a prudent decision.

Directors and officers of a corporation are required to perform their duties in accordance with established legal standards. Since these standards vary considerably from state to state, directors should review the specific laws of their own state. In California, for example, a director must act (1) in good faith; (2) in a manner the director believes to be in the best interest of the corporation; and (3) with such care, including reasonable inquiry, that an ordinarily prudent person in a like position would use under similar circumstances. Thus, if the board of directors decides not to repair broken equipment for financial reasons, and a child is injured by the equipment, the board of directors could be individually sued for failing to make a prudent decision.

A non-profit corporation can protect its directors from liability in the event of a lawsuit by indemnifying the directors in the corporate bylaws. A typical indemnification clause would read:

"This corporation shall, to the maximum extent permitted by law, indemnify each of its present or former directors, officers, employees, or other agents against expenses, judgments, fines, settlements, and other amounts actually and reasonably incurred in connection with any proceeding arising by reason of the fact that any such person is or was an agent of this corporation."

In California, such a clause only provides protection when the director or officer was acting in good faith and in a way reasonably believed to be in the best interest of the corporation. The effectiveness of an indemnity provision will depend on the ability of the corporation to pay for the expenses incurred by the director in defending the suit.

An errors and omissions liability policy will protect board members and officers if they are individually sued. This type of policy has two different provisions—expense reimbursement and directors' liability. If there is an indemnification provision in the bylaws, the errors and omissions policy would reimburse the corporation for the amount it had to pay the directors or officers under the indemnification agreement. If there is no indemnification provision in the bylaws, the errors and omissions policy directly insures the board members, and the corporation is not involved in defense or payment.

- **Broad form comprehensive general liability endorsement.** A broad form comprehensive general liability endorsement can add personal injury, contractual, and a small amount of fire legal liability to your comprehensive general liability policy. Although it is usually cheaper to purchase this endorsement, the provisions and coverage provided by a broad form comprehensive general liability endorsement should be read carefully to make sure that proper coverage and appropriate amounts are included.

- **Excess liability coverage.** This coverage provides excess amounts of coverage above the amounts of the basic general liability insurance policy. For example, if you purchase a $100,000 comprehensive general liability policy from Company A, you could buy an excess policy from Company B. It would provide another $400,000 coverage. The combined total coverage would be $500,000. The second policy would provide extra liability coverage only after the basic policy paid on the claim to its limits. If the primary coverage is adequate, then the excess liability coverage may be relatively inexpensive.

- **Additional insureds.** Frequently, funding sources as well as landlords will require that they be named on your insurance policy as additional insureds. This means that if they are named as co-defendants in a suit against you, the insurance would cover both the cost of their defense and any part of the settlement or judgment against them. The cost of naming an additional insured is typically minimal and is sometimes free of charge.

Transportation Insurance

If your child care center owns or leases any vehicles, automobile insurance is necessary. Bodily injury, property damage, and uninsured motorist protection are mandatory coverages included in an automobile insurance policy.

- **Bodily injury and property damage.** This coverage will pay for any bodily injury or property damage that must be paid as a result of an accident caused by you.

- **Uninsured motorist protection.** This coverage allows the occupants of the insured vehicle to collect from their own insurance company for bodily injuries which are caused by an accident with an uninsured motorist or a hit-and- run driver.

Other optional forms of coverage you may purchase include:

- **Medical payments.** This is a no-fault type of coverage which provides protection for injuries to passengers while riding in a vehicle owned and insured by you.

- **Comprehensive coverage.** This coverage provides protection for physical damage sustained by an insured vehicle, such as vandalism, fire, broken windshields, etc. It will not cover losses caused by collision.

- **Collision.** This coverage provides protection for damage to the insured vehicle when involved in an accident with another car or object.

- **Underinsured motorist coverage.** If you are involved in an accident with someone whose liability insurance does not fully cover the injuries sustained by you or your passengers, you can collect from your insurance company.

How much automobile insurance coverage do you need? Some experts suggest a $300,000 minimum for bodily injury and property damage coverage. A child care center which regularly transports children, however, may want to substantially increase its coverage to protect itself in case of a serious accident. Coverage can be significantly increased without incurring a proportional increase in premiums. For example, $1,000,000 worth of coverage generally costs only about 25 percent more than $300,000 worth of coverage.

If employees' or parents' vehicles are used to transport children, the child care center should still protect itself. Although the non-center owned vehicles are presumably insured by their owner, it is still important for the child care center to make sure that it is adequately covered in the event of a serious accident because it is highly likely that the center itself will be named as a defendant along with the driver.

It is important to note that the car owner's insurance will not cover any liability which could be attributed to the center's negligence. For example, if the accident occurred because the driver was distracted because there were too many children in the car, or there was a lack of adequate supervision, the car owner's insurance will not cover the legal fees of the child care center if the center is named as a co-defendant in a lawsuit.

There are, however, a number of ways a child care center can protect itself when using non-center owned vehicles:

- **Driver requirements.** The center should make sure that the parent, staff, or volunteer is a safe driver and does not have a history of traffic violations. Any car used to transport children should be covered by insurance, preferably at limits significantly beyond minimums many people carry. To make sure the car is insured, you could ask the owner for either a photocopy or a certificate of insurance from the insurance company. To make certain the limits are sufficient, the center might require the driver to increase the limits. Alternatively, if the program is non-profit, it might consider purchasing social service excess liability coverage, described below.

- **Employer's non-owned auto insurance.** An employer can be held liable for the actions of an employee or volunteer while that employee or volunteer is on business for the employer. This coverage will protect the center itself if it is named in a lawsuit arising out of the use of a vehicle owned by an employee or volunteer. If your center regularly uses staff or volunteers to transport children on field trips, this coverage should be considered.

- **Volunteers' excess liability insurance or social service excess auto coverage.** This coverage is available in some states to non-profit organizations which use volunteers and employees as drivers. This coverage will automatically extend the automobile liability insurance of the child care center to protect volunteers and employees when their own cars are used to transport children. It is important to note, however, that this policy only provides coverage over and above the individual's own policy.

- **Hired auto liability.** This coverage is sold as an add-on to the center's general liability policy and provides excess liability above the amount of insurance available from the rental company. This coverage, however, is limited to short-term rental vehicles, and thus is only useful to programs which use rental vehicles to transport children and staff.

How Much Is Enough?

People in insurance recommend a minimum of $500,000 in bodily injury and property damage, but the appropriate amount of coverage will depend on how many children are in your care. Liability insurance is written on either a split limit basis or a single limit basis. In a split limit policy which provides $500,000 bodily injury per person and $1,000,000 bodily injury per occurrence, $500,000 could be paid for any one person injured and $1,000,000 would be paid for two or more persons injured. For example, if the play structure at your center collapsed, protection for bodily injury would be up to $1,000,000 for all persons injured, but no more than $500,000 for any one person. A combined single limit policy will provide protection up to the limit of the policy for any person or up to the limit for a combination of bodily injury and property damage.

Understanding Your Policy: "Claims Made" vs. "Occurrence"

Most general liability policies are *occurrence* policies which means that as long as the policy is in effect at the time of the accident, the policy will provide coverage regardless of when you are sued or whether or not you are still insured with the company. A *claims made* policy requires that the policy be in effect when the accident occurs *and* when the suit is brought against you. Since the long-term effects of an injury may not always be immediately known, it is important to determine whether your policy is *claims made* or *occurrence*.

It is important to read your insurance policy carefully to make sure that all of the provisions are clearly understood. The declaration page should indicate that comprehensive general liability is included. It is also important to note any exclusions in the policy and additional liability coverage which is purchased. Products liability, for example, will be shown as an endorsement on the policy and will define the coverage provided by the endorsement.

There is currently some debate over whether child care services constitute *professional services* requiring a special type of insurance coverage called *professional liability insurance*. If a liability policy specifically excludes or includes coverage for professional services, you should find out whether the insurance policy defines child care as a *professional service* and discuss this with your agent or broker.

Q and A about Physical and Sexual Abuse Liability

Q: Is an employee of a child care center covered under the terms of a general liability policy if accused of physical or sexual abuse?

A: If the employee has been added to the liability policy as an additional insured, or you have a separate employees' liability policy, most liability insurance policies will defend the employee if a *civil suit* is brought against the employee. The insurance company, however, will only provide a legal defense until liability is clear and *will not* pay for any damages if the employee is found liable. If criminal charges are brought for physical or sexual abuse, the employee *will not* be provided with a defense to a criminal charge under a general liability policy.

Q: If an employee of a child care center is accused of physical or sexual abuse to a child in the center, would the child care center itself be covered by the general liability insurance policy if named as a defendant in a civil lawsuit?

A: Unfortunately, there is not a clear answer to this question because cases are currently being decided in this area. Coverage will depend not only on the specific terms of the policy, but also on the particular claim made in the lawsuit. For example, a general liability policy may provide coverage for a suit based on negligent supervision of the employee, but not for a suit based on negligent hiring. The best way for a child care center to protect itself is to discuss the terms of the liability policy with their insurance agent and ask the agent about coverage in this type of situation.

Q: Would directors and officers be covered if individually named in a lawsuit which is brought against an employee of a child care center for physical or sexual abuse?

A: As discussed earlier in this article, a director or officer of a corporation can be held liable for failing to make a prudent decision. The legal liability here would most likely be for negligent hiring if the board member or officer directly hired or approved the hiring of a child care employee accused of physical or sexual abuse. A directors' and officers' liability policy may provide coverage in this situation; but, again, the extent of the coverage varies, and so it is best to discuss this with your agent.

Liability policies can be purchased directly from an agent or broker, or through a child care association. Partly due to recent public attention to abuse in child care settings, some programs are having difficulty purchasing liability insurance at all.

If you are experiencing that problem, contact local, state, and national child care associations for information about group policies or names of insurance companies which are continuing to insure child care programs.

It is possible to insure yourself against almost any possible risk. However, no child care program can afford to go to such extremes. Therefore, it is important that you buy insurance only after a careful assessment of your program's specific needs and budgetary restraints.

References

Chapman, Terry S. et al. **Am I Covered for . . .? A Guide to Insurance for Non-Profits.** Society for Nonprofit Organizations, 6314 Odana Road, Suite 1, Madison, WI 53719 (176 pages, $10.50 prepaid).

Lane, Marc J. **Legal Handbook for Small Business.** AMACOM, 135 West 50th Street, New York, NY 10020 (181 pages, $14.95).

IAC
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John H. Blair
President

July 19, 1985

The Hon. Peter A. Nystrom
116 Broad Street
Norwich, CT 06360

Dear Representative Nystrom:

One of the handouts distributed at yesterday's meeting on day care liability insurance detailed several specific problems involving Connecticut day care providers. Most of these problems involved inadequate notice of non-renewal or increase in premium.

I thought it would be helpful to make you aware that the General Assembly did pass legislation in 1985 which should resolve that part of the problem. Enclosed is a copy of Public Act 85-156 which extends existing requirements regarding notice of non-renewal and notice of premium billing for personal insurance to commercial insurance, which would include day care liability insurance.

I appreciate the opportunity to attend yesterday's meeting and will be happy to work with you in dealing with this issue in the future. If you have any questions about the enclosed Public Act or other elements of this issue, please feel free to call me at any time.

Sincerely,

Mike Meotti

Michael P. Meotti
General Counsel

MPM:ras
enclosure
cc: Jeanne Milstein

AN ASSOCIATION OF CONNECTICUT INSURANCE COMPANIES

Effective [illegible]

Substitute Senate Bill No. 382

PUBLIC ACT NO. 85-156

AN ACT CONCERNING ADVANCE NOTICE REQUIREMENTS FOR NONRENEWAL OF INSURANCE POLICIES AND PREMIUM DISCOUNTS FOR SENIOR CITIZENS.

Be it enacted by the Senate and House of Representatives in General Assembly convened:

Section 1. (NEW) (a) No insurer shall refuse to renew any policy which is subject to the requirements of chapter 682a of the general statutes unless such insurer or its agent shall send, by registered or certified mail or by mail evidenced by a certificate of mailing, or deliver to the named insured, at the address shown in the policy, at least thirty days' advance notice of its intention not to renew. The notice of intent not to renew shall state or be accompanied by a statement specifying the reason for such nonrenewal. This section shall not apply: (1) In case of nonpayment of premium; or (2) if the insured fails to pay any advance premium required by the insurer for renewal, provided, notwithstanding the failure of an insurer to comply with this subsection, with respect to automobile liability insurance policies the policy shall terminate on the effective date of any other insurance policy with respect to any automobile designated in both policies.

— would include day care liability insurance (and already covers homeowners which may have rider)

Notice of non-renewal 30 days

(b) A premium billing notice for any policy subject to the requirements of chapter 682a, except a workers' compensation policy, shall be mailed or delivered to the insured by the insurer or its agent not less than thirty days in advance of the renewal date or the anniversary date of the policy. The premium billing notice shall be based on the rates and rules applicable to the ensuing policy period. The provisions of this subsection shall apply to any such policy for which the annual premium is less than ten thousand dollars.

Notice of premium billing 30 days

(c) Failure of the insurer or its agent to provide the insured with the required notice of nonrenewal or premium billing shall entitle the insured to: (1) Renewal of the policy for a term of not less than one year, and (2) the privilege of pro-rata cancellation at the lower of the current or previous year rates if exercised by the insured within sixty days from the renewal date or anniversary date. Renewal of a policy shall not constitute a waiver or estoppel with respect to grounds for cancellation which existed before the effective date of such renewal.

discount of five per cent shall be applicable to premium charges for such automobile for policies effective on and after July 1, 1983, [, but before January 1, 1986.] The discount shall apply to the premium charges for the automobile for at least twenty-four months. This section shall not apply to any group automobile insurance policy issued pursuant to section 38-185n under which premiums are broadly averaged for the group rather than determined individually.

(b) The commissioner of motor vehicles shall adopt regulations in accordance with the provisions of chapter 54 concerning the content and other requirements of the accident prevention course referred to in subsection (a) of this section, including, but not limited to, the number of hours of classroom instruction, approval of schools and instructors offering the course and certificate issuance upon successful completion.

Sec. 5. Sections 38-175i and 38-175o of the general statutes are repealed.

Certified as correct by

____
Legislative Commissioner.

____
Clerk of the Senate.

____
Clerk of the House.

Approved ______________________________, 1985

____
Governor, State of Connecticut.

STATEMENT OF J. ROBERT HUNTER, PRESIDENT, NATIONAL INSURANCE CONSUMER ORGANIZATION, ALEXANDRIA, VA

Mr. **Hunter**. Thank you, Mr. Chairman.

Chairman **Miller**. Your statement will be included in the Record and you'll have an opportunity to read it. In addition, please respond if you can to some of the things that were said by the previous panel. It would be very helpful.

Mr. **Hunter**. I'd like to do that, sir. And what I would propose doing is just to refer to the charts in the back of my statement for a moment, just to put it into context. On the last page of my statement, I show a chart which shows the underwriting cycle, the cycle of profitability of the insurance industry over the last 25 years, and you can see that there is a cyclical pattern to it, and as other witnesses have testified, we are at a bottom. In 1984, the profit was only 3 percent. There was not a loss in 1984, but 3 percent rate of return on net worth is about at historical bottom levels.

The stock market has responded very positively. Chart No. 2 shows that the Best Property Casualty Index is at an all time high. The National Underwriter, just this week, July 26 edition, points out that the general market Dow Jones industrial average stock went up 10 percent. The Standard & Poor's 500 lists the first half of 1985, the Standard & Poor's 500 went up 15 percent, the NASDAQ composite went up 20 percent, the multiple line insurance companies, which are the big Aetnas and AIG and people like that, went up 33.5 percent.

The property casualty insurance industry stocks went up 27.4 percent to all time record highs. The cycle is an anticipated economic phenomenon in the insurance industry. Chart No. 3 shows that even during a time of minimal profits, the cash flow of the underwriters is great.

I'd like to read a couple statistics just to put it into perspective; this is from Best's Advance Rating Report of July 15. The net cash flow for 1984, in other words the money the insurers had to invest, and so on, at the end of the year was $11.8 billion more than they had the previous year.

This is the property casualty insurers. The surplus we've heard so much about, in 1980, was $52.5 billion; currently it's at the end of 1984, it was $63.8 billion. a significant increase in surplus. There was a drop from 1983 to 1984, of just a little over $1.6 billion from $65.4 to $63.8, but according to reports on the first quarter, that's been recouped in the first quarter of 1985.

So, I don't think there's a major catastrophe in the insurance industry. Surely they are at the bottom of the cycle.

I happen to have been Federal Insurance Administrator during the last bottom of the cycle, and I sat in hearings like this, saying what are we going to do about medical malpractice and product liability insurance? And I testified before Senator Kennedy on the Health Committee, for example, stating that the thing to do is to try to do something about the cycle, that the crisis is one of short term character every few years at the bottom.

In fact, that turned out to be the case. As soon as the cycle swung up, as you see on the chart (the cycles go up and down)—all this talk about crisis disappeared. In fact, the underwriters fell all over themselves to cut the prices of the very lines of insurance that we now hear are such a catastrophe.

Let me read from a National Underwriter Report in 1981, November 20, that I have in my statement. This is a quote. "A large commercial umbrella liability risk [this would be the very kind of risk we're hearing is so terrible] came up for renewal and was rated at $105,000 about the same as the previous year but the insured was not satisfied. Aware of the aggressive rate competition in the commercial lines market, he decided to shop around. He approached a second agent which offered a $20,000 premium, but the insured was still not happy, and he continued to shop, and eventually the original company which originally wanted $105,000 came back and took the business for $5,000. That's right, $5,000!"

That's the kind of rate cutting that was going on in this line in 1974, they were saying liability insurance is going to hell in a handbasket, and we've got to change all the tort laws and we've got to do all these other things, blaming everybody but themselves, and then five years later, they're cutting the prices like that.

In 1981, you may remember the MGM Grand Hotel fire: they got liability insurance after the fire, so not only were they willing to write liability insurance, they were willing to write liability insurance after the liability had already happened. In fact they just paid out $76 million on that claim which is, if my calculations are correct, 13 times the claims for all the day care centers in the ISO exhibit for last year.

So, what happens at the top and bottom of the cycle is what I call an industry manic depressiveness. The insurance industry will do almost anything, give away, you know, toasters and everything to get your insurance at the top of the cycle; at the bottom of course, anybody, no matter how good they are, can't get insurance. And I think it's pretty bad that the States that allow this to happen, come here and testify like they're wringing their hands, they have a responsibility to keep rates adequate, not excessive and not unfairly discriminatory, and what happens clearly at the top of the cycle is these rate cuts lead to inadequate rates and the states don't do anything about it.

And at the bottom of the cycle, what's going on right now, we're having rates that are clearly excessive.

[Prepared statement of Robert Hunter follows:]

Prepared Statement of J Robert Hunter, President, National Insurance Consumer Organization, Alexandria, VA

Mr. Chairman and members of the Select Committee, I appreciate your invitation to talk to you today regarding the mounting problem faced by day care providers in obtaining reasonably priced liability insurance.

The general insurance situation—its impact on day care insurance:

The collage of insurance related headlines attached to my testimony is stark evidence of a general insurance turmoil which has engulfed the day care providers of this nation, along with nurse-midwives, fishermen, towns, states and others.

Why?

The first chart shows a very important fundamental which you need to understand if you are to understand the 1985 insurance situation. It shows the cyclical nature of profits in this major and vital industry.[1]

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[1] Source of data: Citybank Economics and Insurance Services Office.

The property/casualty (p/c) industry is at the bottom of the cycle. Its profits are about at traditional lows based on recent cycle bottoms of 1974/5, 1969 and 1964/5. Wall Street is not concerned (see Chart 2), recognizing the usual pattern is in place for a sharp recovery over the next 18 months.[2] Wall Street also is aware that the low profits do not mean the end of available investment dollars, put away at a $10 billion clip even in 1984 (see chart 3).[3]

Insurance executives tend to overreact at the bottom of the cycle, however. Under some pressure from boards of directors to do something, they have rather ritualistically in recent cycles blamed the problem on a convenient whipping boy, the lawyers and the courts. This scapegoat tactic led to tort law changes in most states after the 1974/5 crises in medical malpractice and product liability,[4] many of which sharply curtailed victim's rights (as Federal Insurance Administrator, I was proud of having participated in getting Presidents Ford and Carter to support no-fault auto insurance, but the "reforms" sought by insurers in the current context appear to be simply profit centered, not in the best interests of our citizens. They are seeking "reform" under the gun of cancellation and rate hike, rather than logic and study).

The last cycle bottom was most informative. I was, as Administrator, able to serve on interagency groups that studied the phenomena. We found that the crises were in the minds of the underwriters much more than in the claims as we collected and analyzed the data. The testimony I gave before Senator Kennedy's Health Subcommittee concluded that ratemaking had run amok; the report of the interagency task force on product liability concluded that the insurers engaged in panic pricing.[5]

While the industry executives act in an overly pessimistic way at cycle bottom, the reverse is true when times are good. At the top of the cycle the insurers undertake what they themselves call "cut-throat" tactics to gain the cash flow for investment purposes. Large buyers of insurance, not the little buyer unfortunately, were reported in the trade press as obtaining rate cuts of up to 90%.[6]

At the top of the cycle the scapegoat is forgotten and tort reform is sidelined as insurers chase the cash. The zenith of this chase was the purchase of $165 million of liability insurance by MGM for its Grand Hotel fully 3 months after the fire.[7] The reason for this is simple, although the insurers now complain about the "long tail" of liability claims, they love the long time they get to hold reserves in double digit interest rate securities before they pay out the claim.

So the availability and price of insurance is wildly dependent upon the attitude of the underwriters, and that is largely driven by the underwriting cycle, itself largely driven by the underwriters' somewhat irrational behavior at the extremes of the cycle.

America surely needs the stability that insurance normally brings to the economic activities of our citizens. When insurance acts to destabilize, however, it is high time that the Congress carefully consider ways to flatten the cycle or address the symptoms, unavailability or unaffordability of insurance to decent risks through no fault of their own.

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[2] Source of data: Best's Property/Casualty Stock Index, A.M. Best and Co., Oldwick, NJ.

[3] Source of data: A.M. Best and Co., Oldwick, NJ.

[4] St. Louis Post Dispatch, section B, p. 3, April 14, 1984.

[5] Hearing of December 3, 1975, Subcommittee on Health of the Committee on Labor and Public Welfare, U.S. Senate. Among the interesting data supplied by ISO at that hearing were exhibits that showed that the average claim cost ISO used for ratemaking significantly exceeded the limit of liability, clearly ratemaking that had run amok. That led to this exchange:

Senator LAXALT. Is malpractice always a loser as far as carriers are concerned?

Mr. HUNTER. If they charge these rates, they could not help but win. (p. 141)

In John Gunther's book, *The Malpractioners*, Anchor Press, 1978, Gunter cites this exchange at p. 169 in a chapter entitled "They Could Not Help But Win". In the following chapter, called "They Won", Gunther reviewed the later experience.

Final report, Product Liability Task Force. *Report on Product Liability Ratemaking*, Product Liability and Accident Compensation Task Force, U.S. Department of Commerce, 1980. At p. ix the report states that "overly subjective ratemaking practices were one of the principal causes of the product liability insurance problem."

[6] See, for instance *National Underwriter*, November 20, 1981, p. 1, where it says:

"A large commercial umbrella (liability) risk came up for renewal and was rated at $105,000, about the same as the previous year. But the insured was not satisfied. Aware of the aggressive rate competition in the commercial lines market today, he decided to shop around. He approached a second agent, who submitted the very same risk to a different company, which offered to write it for just $20,000."

But the insured was still not happy. He continued shopping and eventually *the original company, which originally wanted $105,000 came back and took the business for $5,000. That's right, $5,000.* [Emphasis added.]

[7] *Journal of Commerce*, February 18, 1981.

The day care experience—does this line deserve to be treated as it is?

The answer is "no".

At your last hearing, the insurers did not testify. I hope that will be rectified today. The testimony of the providers gave no basis to expect that the "crisis" is anything more than more overreaction to the cycle bottom, coupled with some untimely publicity vis-a-vis child abuse.

The only data I've seen is from the Insurance Services Office (ISO), the industry cartel-like organization which can exist to make joint rates because of this industry's unique exemption from the federal anti-trust laws.[8]

The ISO data is for four years. The data does not show how many day care facilities were included in the data, but it is represented to be data for all companies reporting to the ISO, a significant percentage of the data in the nation.

The data show that for the four most recent years (1980-1983) there were 1,121 claims filed in the entire country. That would be about 5.5 claims per state per year. If we assume that insurer expenses and investment income offset (a fair assumption for this line of insurance), the industry probably lost about $500,000 or about $2,500 per state per year.

Even looking at the worst year, 1983, the data don't look like a crisis. At the very worst, a rate change of up to 100% might be called for for 1986. If I were asked by a state to make an actuarial judgment on the basis of that data, I'd recommend about a 50% increace. The limit on the change an actuary recommends is based on the believability of the data, something we actuaries call "credibility". There are insufficient data in the ISO countrywide day care experience to afford these data full believability. Similarly, there's no way that cancellations or increases of 200% up are justified.

Let's put this line in perspective to see just how irrational the cancellation/nonrenewal/large price increase behavior of the insurers appears to be. Assuming that the dollars of claims incurred as reported by ISO actually are paid out at the level they project (even this takes quite a leap of faith; it is likely that less than $1 million of the ISO reported $5 million in claims is actually paid out as of now—we don't even know what the size of the adjustments ISO made to the data are), the total national 1983 day care incurred losses would be: .004% of the premiums written by the p/c industry; .008% of the surplus of the p/c industry; .11% of the p/c premiums written by Aetna Life and Casualty, a leading writer of day care liability in the past; and incredibly, the entire incurred losses for the country's day care providers as reported to ISO is only about 6% of the losses paid out on the MGM Grand Hotel under the policy entered into after the fire, mentioned earlier.[9]

The panic has to be related to spectres of large verdicts in the wake of the recent publicity on child molestation . . . it is certainly not found in the data provided to date.

What is the nation to do about these abusive insurer practices?

NICO believes that the approach enacted at a previous bottom, 1968/9 is worthy of consideration by the Congress: The Urban Property Protection and Reinsurance Act of 1968 was a response to the unavailability of insurance in the inner cities in the wake of the riot situation of the late 60's.[10]

To be sure, the predicate for the withdrawal of riot insurance was strong, given the very serious situation extant in the country at the time. But the finding of the President's Panel on the Insurance Crisis is just as valid for the day care provider community today as it was for the inner city communities of the late 60's: "Communities without insurance are communities without hope".[11] Providers will have to shut down, possibly forcing spouses to decide among themselves which one will have to stop working, or the latchkey situation will be exacerbated, or other undesirable results will be forced on parents. Some families may even have to give up a home for loss of the second income, situations not unlike the loss of mortgage following loss of insurance in inner city areas plagued by riot almost two decades ago.

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[8] Data submitted to the Select Committee by ISO. For a full discussion of the role of rate bureaus in the insurance industry, and their anti-competitive nature, see *Investment Income and Profitability in Property Casualty Insurance Ratemaking*, a report to the National Association of Insurance Commissioners, J.W. Wilson and J.R. Hunter, January 1983.

[9] Sources: Premium and surplus, A.M. Best and Co.; Aetna data, Aetna Life and Casualty as reported by A.M. Best and Co.; MGM Grand Hotel Settlement *Business Insurance*, April 8, 1985, p.1. According to the article, MGM received a total recovery from insurers of $115.5 million of which only $30 million was from the non-retroactive normal liability insurance the Grand Hotel had at the time of the fire.

[10] Public Law 90-448, 82 Stat. 476; 12 U.S.C. 1749bbb, 42 U.S.C. 4011.

[11] *Meeting the Insurance Crisis of Our Cities*, A report of the President's National Advisory Panel on Insurance in Riot-Affected Areas, January 1968, p. 1.

The federal government agreed to reinsure (insure the insurance companies—a sort of lay-off bookie arrangement) the insurers against the specified peril of riot and civil commotion in return for a reinsurance premium and a commitment to participate in a pool to make sure insurance is available to all residents whose homes met reasonable standards of insurability.

The federal government made $125 million writing this reinsurance!

The cities were saved from the sure death that no insurance brings in twentith century America!

The program worked well.

I think that a program of stand-by authority should be prepared to take care of the day care and nurse-midwives current problem (and, perhaps some of the others). The authority should be granted to cover future crises as well, to stabilize the insurance profit cycle's harsh symptoms.

When a line of insurance became severely distressed, representatives of those purchasers could appeal to the agency given authority to reinsure. The agency would make a finding as to the extent and cause of the dislocation. If a distressed situation is certified, then the agency could offer reinsurance to insurers who would agree to make a market in the line. Following meetings with the insurers, the agency head would determine what the cause of distress was and would offer only to reinsure that cause (e.g. only reinsure the peril of child abuse for day care liability if that is the finding). Insurers would pay a reinsurance premium designed to be self sufficient.

Insurers, the administrator of the program and representatives of the distressed industry would meet to set standards for insurability under which those who qualify are assured of an insurance market.

Studies will be undertaken to determine if other longer range action (risk management, tort reform, etc.) is also needed to resolve underlying problems.

Funding for this program would come from reinsurance premiums. I also envision a small surcharge, perhaps one-quarter of one percent of premiums written by all p/c insurers, to back up the program. This is in case premiums are insufficient over a short period or if it is determined by Congress that some short term subsidy is required to stabilize a distressed line sometime in the furure.

The one-quarter of one percent surcharge would cost only 81 cents on the average private passenger car premium but would yield over $300 million this year. Over a ten year cycle, with a 10% growth in premiums and a 10% interest rate, $7 billion would flow into the Treasury. I would envision these funds being used in the general revenue area, but carefully accounted for to be available to the agency head when needed.

CONCLUSION

America deserves a better deal on its insurance. The federal government cannot sit idly by and let the insurance industry hold day care providers hostage in a larger game beyond the providers' control. The terrorist tactics of insurers every 10 years at cycle bottom must be dealt with in a systematic way that adds the stability to our economy that insurance is meant to deliver. It is time the Congress began to look at the delegation it made to the states in 1945 to see if we are, as a nation, getting the most we can out of that twelve percent of our disposable income we pay into insurance premiums. A good place to start is solving the day care crisis that exists only in the minds of a few underwriters on John Street in New York City.

I welcome any questions you may have. I offer the full assistance of NICO to you in your efforts on behalf of the oppressed providers of our nation's child care.

CHART #1

THE "CYCLE" AND CONSUMER ABUSE

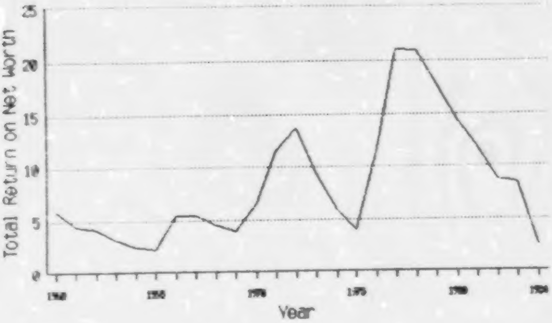


CHART #2

Best's Property/Casualty Stock Index

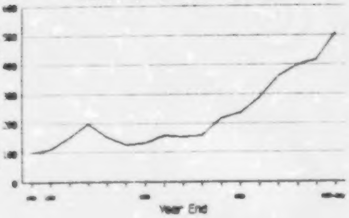
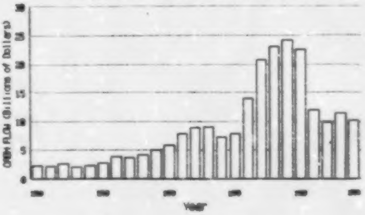
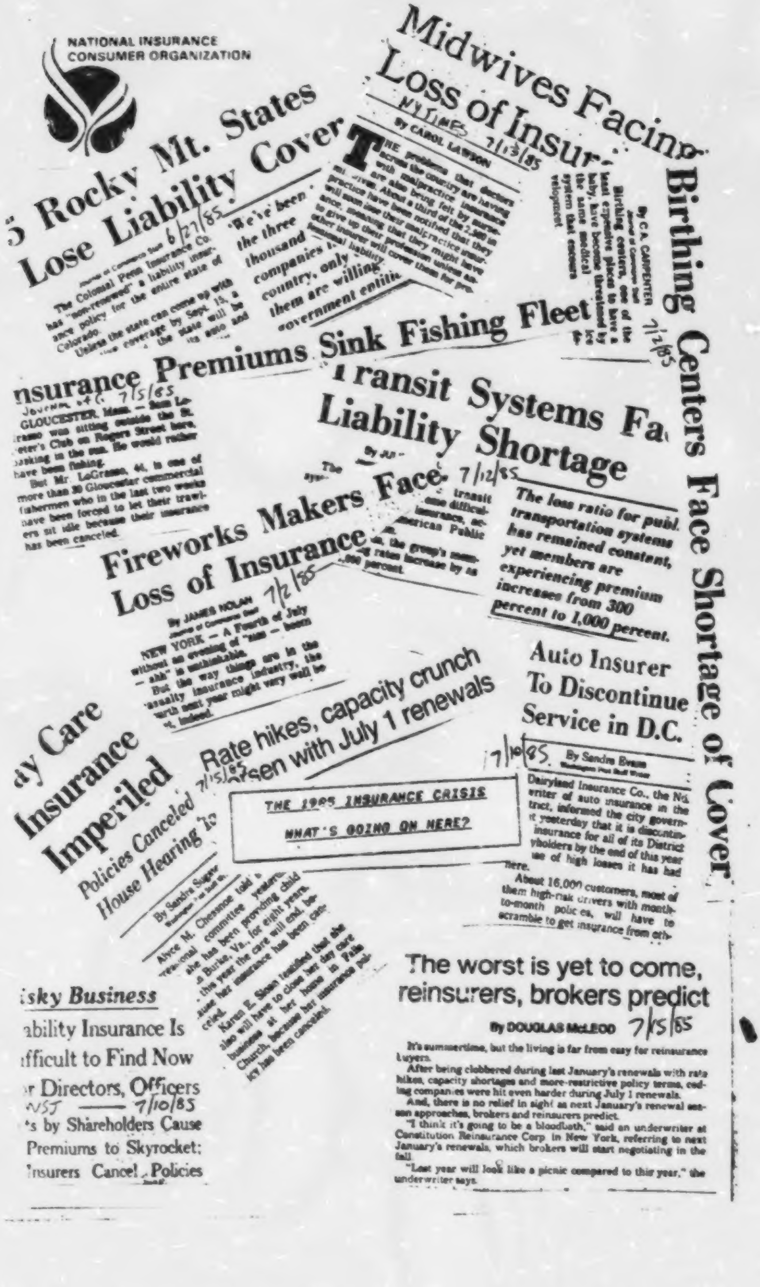


CHART #3

CASH FLOW OF INSURERS





NATIONAL INSURANCE
CONSUMER ORGANIZATION

5 Rocky Mt. States Lose Liability Cover

6/27/85

The Colonial Penn Insurance Co. has "non-renewed" a liability insurance policy for the entire state of Colorado.

Unless the state can come up with coverage by Sept. 15, a the state will be its auto and

'We've been the three thousand companies i country, only them are willing government entitie

Midwives Facing Loss of Insur

NY TIMES 7/13/85

By CAROL LAWSON

THE problems that doctors across the country are having with malpractice insurance are also being felt by nurse-midwives. About a third of the 2,500 in practice have been notified that they will soon lose their malpractice insurance, meaning that they might have to give up their profession unless another insurer will cover them for pro

Birthing Centers Face Shortage of Cover

7/12/85

By C.A. CARPENTER

Birthing centers, one of the least expensive places to have a baby, have become threatened by the same medical system that concern velopment

Insurance Premiums Sink Fishing Fleet

JOURNAL of C. 7/5/85

GLOUCESTER, Mass. — Sam LoGrasso was sitting outside the St. Peter's Club on Rogers Street here, basking in the sun. He would rather have been fishing.

But Mr. LoGrasso, 44, is one of more than 30 Gloucester commercial fishermen who in the last two weeks have been forced to let their trawlers sit idle because their insurance has been canceled.

Transit Systems Fa Liability Shortage

7/12/85

The loss ratio for publ. transportation systems has remained constant, yet members are experiencing premium increases from 300 percent to 1,000 percent.

transit difficul insurance, ac American Public the group's mem rates increase by as 000 percent.

Fireworks Makers Face Loss of Insurance

7/2/85

By JAMES NOLAN

NEW YORK — A Fourth of July without an evening of "ooh — aah" is unthinkable.

But the way things are in the casualty insurance industry, the Fourth next year might very well be, indeed.

Rate hikes, capacity crunch worsen with July 1 renewals

7/15/85

Auto Insurer To Discontinue Service in D.C.

7/10/85

By Sandra Evans
Washington Post Staff Writer

Dairyland Insurance Co., the No. writer of auto insurance in the trict, informed the city government yesterday that it is discontinuing insurance for all of its District policyholders by the end of this year use of high losses it has had here.

About 16,000 customers, most of them high-risk drivers with month-to-month policies, will have to scramble to get insurance from oth

THE 1985 INSURANCE CRISIS

WHAT'S GOING ON HERE?

Day Care Insurance Imperiled

Policies Canceled House Hearing To

By Sandra Sugawara
Washington Post Staff Writer

Alyce M. Chesnutt told a congressional committee yesterday she has been providing child care in Burke, Va., for eight years, this year the care will end, because her insurance has been canceled.

Karen E. Sloan testified that she also will have to close her day care business at her home in Falls Church, because her insurance policy has been canceled.

The worst is yet to come, reinsurers, brokers predict

By DOUGLAS McLEOD 7/15/85

It's summertime, but the living is far from easy for reinsurance buyers.

After being clobbered during last January's renewals with rate hikes, capacity shortages and more-restrictive policy terms, ceding companies were hit even harder during July 1 renewals.

And, there is no relief in sight as next January's renewal season approaches, brokers and reinsurers predict.

"I think it's going to be a bloodbath," said an underwriter at Constitution Reinsurance Corp. in New York, referring to next January's renewals, which brokers will start negotiating in the fall.

"Last year will look like a picnic compared to this year," the underwriter says.

Risky Business

Liability Insurance Is Difficult to Find Now For Directors, Officers

WSJ 7/10/85

Suits by Shareholders Cause Premiums to Skyrocket; Insurers Cancel Policies

Chairman **MILLER**. May I interrupt you?

Mr. **HUNTER**. OK.

Chairman **MILLER**. There is the suggestion that this cycle is a natural phenomena, but that may not be so. What you're suggesting is that predatory practices are involved.

Mr. **HUNTER**. Correct.

Chairman **MILLER**. To secure market shares, to secure business at the top of the cycle when they're fat and sassy.

Mr. **HUNTER**. Correct.

Chairman **MILLER**. And then, if the rates were inadequate as we were told in 1980, by 1985 they catch up with themselves. What we see is that people have been told, as Senator Nystrom just talked about, that they must absorb a 1,000 percent increase. Those stories have been told now, time and again. We're not just making up for new found liability; we're making up for a history of business practices which have plunged the insurance industry as a whole into a downward cycle.
cycle.

Mr. **HUNTER**. That's correct.

Chairman **MILLER**. You're suggesting that they have an aversion to stability in this industry.

Mr. **HUNTER**. I think that's correct. I think, my definition of them as a manic depressive is accurate. At the top, they do crazy things in terms of cutting prices, particularly in the commercial lines where the commercial lines have the ability to self-insure; they don't do such crazy things in personal lines. Competition is very weak in the personal lines, auto and fire insurance and the like, but in these commercial lines [where the particular big buyers of insurance are] is where the giveaways like this $105,000 price down to $5,000 occur. And we pay the price for that at the bottom of the cycle.

And the cycle is exacerbated by the fact there's no control at either the top or the bottom. Commissioner Muhl's statement to the contrary notwithstanding, I can assure you, since I'm an actuary and I've been to several States recently, I can assure you that the States are not looking at day care center price increases.

Chairman **MILLER**. Well, the only thing we know about the cycle is that once again, the consumers are going to fall on the insurance company's sword.

Mr. **HUNTER**. That's correct.

Chairman **MILLER**. It's just a matter of time.

Mr. **HUNTER**. That's correct. And it's Congress' fault.

You delegated the authority to the States to regulate this industry.

Chairman **MILLER**. Well, in that sense, you're right.

Mr. **HUNTER**. With no standards.

Chairman **MILLER**. We delegated them the authority and they refused to exercise it.

Mr. **HUNTER**. Well, it was delegated in 1945 with no standards for performance and I think you've paid the price.

Chairman **MILLER**. If I had known that in 1945, I would have changed it.

Mr. **HUNTER**. Well, what I wanted to say is, looking at the day care centers, I had the same experience that we've looked at, and the question I tried to answer is: Does this line deserve to be treated as it is being treated, and in my statement I say it does not.

At the last hearing, we didn't hear much about experience. This hearing we got some experience, and I'm more convinced than ever—I had already seen this experience—and I, as an actuary, would say yes, they probably need a rate increase, maybe as much as 100 percent maximum. I would recommend if I was a consulting actuary to a State or something, I would recommend probably something on the order of a 50 percent rate increase.

But the idea that they'd have to cancel any of these is beyond the pale, and I do believe, of course, that they should cancel ones that have real bad records or something like that, but I'm saying wholesale cancellations just make no sense at all from a technical viewpoint or from a public policy viewpoint. I point out that the entire losses represent four one-thousandths of 1 percent of the premiums written by this industry.

Eight one-thousandths of one percent of the surplus in the so-called declined surplus, 0.1 percent of the premiums written by Aetna Life Casualty, who are a leading writer; they could take the whole loss themselves and not charge a premium and hardly notice it on their annual statement.

And as I said, it's 13 times what was just paid out on the MGM fire, so we're talking about such a minor amount of money to this industry that it's incredible that they've allowed this thing to get out of hand. It is hysteria; it is in their minds; and in part, it's a panic that they go through for their own self interest because, in effect, in 1974, I had an insurance commissioner grant a rate increase of 100 percent and I went to see him.

I said, the data only shows maybe a 20 percent rate increase for medical malpractice, and the commissioner said, yeah, that's what we told the company but then the company said—and it was the only company writing—we're going to pull out if you don't give us 100 percent, and suddenly I found the actuarial accuracy of their calculation was okay. Obviously he was intimidated into approving the 100 percent rate increase.

And there is an intimidation factor in this and it's meant to intimidate not only the State insurance commissioners but also legislators viz-a-viz the tort reform issue. And I got two Presidents to support nofault auto insurance, when I was Federal Insurance Administrator so I'm not against tort reform, but I am against tort reform under a gun like this . And I think they were crying for the same kind of tort reform in 1974, and 1975. The problem went away by itself; I would predict that the problem will be gone in 18 months, so I guess I'm sort of between Commissioner Muhl's 1-year prediction—I hope he's right—and the industry's 3-year prediction. But I would say within 18 months, we won't hear any more about tort reform or anything else, and in fact, we'll be wondering how they're making so much money.

But I do appreciate the opportunity to testify today sir.

Chairman **Miller**. Well, let me suggest that if your testimony is accurate that what we have at its worst is a conspiracy between the companies and the insurance commissioners to fail to police adequately the rates and premiums that are charged over a long period of time, and at best what we have is an hysterical reaction by the insurance industry that is unfairly burdening the child care industry and the result is that millions of children and their families are being placed at a much greater risk.

Mr. **Hunter**. I didn't go so far as to——

Chairman **Miller**. And the purpose of these hearings has been to try to get evidence for the industry to justify the treatment of the child care industry. And I have to say, as we near the close of the second set of hearings, that evidence just isn't there.

I appreciate the economic evidence that was submitted this morning about the trials and tribulations of the insurance industry on a nationwide basis, but it still doesn't seem to me that it should translate into the kind of treatment the child care industry has received.

As we will hear from Mr. Birch, the issue of abuse in child care has been overblown, both in the press and in the minds of the insurance industry.

Mr. **Hunter**. Well, I agree with you. I think that it is hysteria and I think it is falling on the day care centers and others. My testimony has a collage of headlines, you probably noticed, because I mean people are just being abused generally. And I wouldn't go so far as to——

Chairman **Miller**. From what it appears, the child care industry's being abused, that's what's going on.

Mr. **Hunter**. Well, as far as the insurance industry, it's a self-afflicted problem that they have and to take it out on day care centers is just wrong. That's why I proposed in my statement which is rather technical, that some kind of reinsurance by the Federal Government to ease the bottom of these cycles might be appropriate, as a standby authority, and not only for day care centers by 1995 (the next time we sit here and go through this same kind of a mess); 12 percent of the disposable income is paid into insurance premiums, I don't think the Congress should sit by and let that 12 percent kind of dig into the whole country every 10 years.

Chairman **Miller**. One of the things that concerns me is the suggestion is that the insurance industry can sell liability insurance where it is required to, to child care providers, but in fact, they'll end up with a policy that does nothing by the time you get done with the exclusions and the lower limits of liability. I remember once I bought an insurance policy for my son, and when I got done, I paid three times as much as I had paid before he'd gotten into his accidents, and I had a policy that met the legal requirements of the law but it had $100 million deductible or something. The policy did nothing.

Mr. **Hunter**. That happens in title insurance every day.

Chairman **Miller**. I'm just concerned that one of the results here, if we act too quickly because of the kind of economic data that comes forward from the industry, that we'll be too quick to provide for exclusions and limits to liability. We will be misleading parents as to the adequacy of the liability coverage that the centers will have.

Mr. **Hunter**. And the other thing that concerns me greatly from hearing the testimony this morning, is that it sounds like Lloyds of London can call the shots on what we do in this country viz-a-viz our insurance mechanism. I don't think that should be.

Chairman MILLER. They're just treating the United States like we're treating the child care centers. Again, a lot of their problems aren't related to the United States casualty market.

Mr. HUNTER. That's correct.

Chairman MILLER. They made some pretty bad decisions.

Mr. HUNTER. That's correct, it's mismanagement and everybody would like to blame somebody else when things go wrong. Of course, why not the tort law, why not the United States?

Chairman MILLER. Tom?

STATEMENT OF THOMAS L. BIRCH, LEGISLATIVE COUNSEL, NATIONAL CHILD ABUSE COALITION, DISTRICT OF COLUMBIA

Mr. BIRCH. Thank you, Mr. Chairman. I appreciate the opportunity to appear before the select committee today and present testimony on behalf of the National Child Abuse Coalition.

We've all heard and are familiar with the stories in the news about the sexual abuse of children in day care programs that for well over a year now have shocked the nation and frightened parents, and lately as this committee has heard during these 2 days of hearings, apparently convinced insurers into believing that children in this country put in child care programs by their parents are in grave danger of being molested.

The fact is, information on reported child molestation refutes the presumption that children in day care are at high risk of sexual abuse. The data we have do not support that notion. What's more, advocates for the prevention of child abuse see day care as an important effort to help prevent the abuse of children, which is the reason why citizens and communities across the country are actively working to make sure that children in day care are not in danger.

Child abuse and neglect is a national problem of huge proportions. Over 1 million documented cases are reported in the United States each year, and this committee is well aware of the tremendous yearly increases in reports of abuse. According to the American Humane Association, which compiles annually national child abuse and neglect reporting statistics, the number of children reported to child protective service agencies increased 121 percent in this country between 1976 and 1983.

I would suggest that that increase reflects the increased public awareness of child abuse, enactment of child abuse reporting statutes encouraging people to report suspected cases of abuse, and the development of programs for treating children who have been abused and working with their families. In its 1983 survey, American Humane looked at figures which reported that 1,007,658 documented cases of child abuse and neglect had occurred. That was an increase of 8.4 percent over the previous year.

Another survey conducted early this year by the National Committee for Prevention of Child Abuse estimated that for 1984, reports rose again, this time by 19 percent, to 1,273,000 children abused and neglected in this country. The number of children included in these reports who have been sexually abused has increased each year also but at a greater rate. Up by 23 percent in

1983 according to American Humane, and an increase of 35 percent last year reported by the national committee.

Now, obviously, this is not an appealing story, but what does it mean about the risk of children being sexually abused in day care programs? American Humane tells us that in 1983, and this is the year for which the most recent figures are available, child sexual maltreatment accounted for 8.5 percent of the reported cases of child abuse and neglect. That is, of the 1,007,000 documented reports of all types of child abuse and neglect, slightly more than 8,500 children were sexually maltreated that year in 1983.

According to the information we have, most of those children were sexually abused in their homes by parents. The statistics show that in 97.1 percent of the cases I've mentioned of sexual molestation, a parent or some other relative is the sexual molester.

The remaining 3 percent of the perpetrators are grouped together and the category includes babysitters, teachers, neighbors, strangers, friends of parents, and staff of State institutions and private institutions. American Humane estimates of that 3 percent category, between 1 and 1.5 percent of the reported perpetrators of child sexual abuse fall into the category of day care employees.

This information should help, I think, put into perspective, the problem of sexual abuse of children in day care programs, a problem much enlarged in the public's mind by news coverage given to the cases that have occurred. The data enforce the belief that child sexual abuse is increasing in this country but that sexual maltreatment of children by day care workers is a very small piece of the problem.

As I've said, those who are working to prevent child abuse believe that child care is an integral part of the prevention effort by helping to support families and strengthen them. In fact, in most subsidized child care, abused and neglected children have first priority for service.

Good child care services can fill many of the goals of a child abuse prevention program enhancing ties between parents' and children, increasing parent skills in coping with the responsibilities of raising their children, reducing family isolation, increasing peer support, and so forth.

Without optimal child care services, I would say that the risk of child abuse in fact increases. Day care center teachers in fact help parents learn better how to care for their children. Parents who've abused their children or may be liable to abuse often have unrealistic expectations of their children's capabilities. Day care teachers can help mothers and fathers understand a child's normal behavior and show parents how to cope with raising children.

Because day care is so important not only as a part of the effort to prevent child abuse but as a basic service required by the families of millions of children across the country day care providers, public officials including the chairman of this committee and members of the select committee, and child abuse prevention advocates have joined forces to ease the minds of parents with children in day care and to protect those children by preventing abuse, sexual molestation in day care from ever having the chance to happen.

The most effective method of preventing child sexual abuse is to educate parents, children, teachers, and day care staff to recognize, to resist and to report sexual abuse. I'd like to mention some of the steps that are being taken to make sure day care is safe for children.

The passage last year of Public Law 98-473, legislation offered by Chairman Miller, provided $25 million to States for child sexual abuse prevention training. This is an extremely important measure in the national prevention effort. A recent report of the National Association of Public Child Welfare Administrators gives some indication on how States are responding to this new source of funding.

Forty-six States, in a survey, said that they planned to provide training in sexual abuse prevention. The new law, as you well know, I'm sure, also requires States to set up criminal record and back ground checks on day care employees. Prior to this Federal mandate, only three States had comparable laws. But since last year, with the passage of Public Law 98-473, over half the States have enacted or are considering such legislation.

I'd mention too a report of the Inspector General from the Department of Health and Human Services in January 1985, reporting on preventing sexual abuse in day care programs, recommended that, as a first priority, HHS should support the kind of educational programs I've tried to describe in my testimony. Which is why we were disappointed when the administration's fiscal 1986 budget proposed eliminating the $25 million to States for sexual abuse prevention training.

We've been encouraged, Mr. Chairman, by your leadership joined by your colleagues on this committee and in the House, to make sure that Congress provides this much needed support another year.

In private organizational efforts, the National Committee for Prevention of Child Abuse has collaborated with Marvel Comics to produce a special "Spiderman" comic book, showing children how to protect themselves from child molestation. Parents anonymous, a national voluntary self-help group, has initiated community sexual abuse prevention forums beginning in southern California, for parents who wish to learn more about protecting their children from sexual abuse.

Scores of films, books, school curricula, plays and brochures have been developed by local organizations all over the country to teach parents and children about preventing sexual abuse.

I have a booklet published this year by the National Committee for Prevention of Child Abuse called Child Care in the Family, and it discusses the importance of child care as a child abuse prevention activity and also includes suggestions for parents about how to shop for day care programs and tips on how to prevent children from being abused. And I'd ask that this be included in the hearing record, Mr. Chairman.

Child Care and the Family

David B. Friedman, June S. Sale, and Vivian Weinstein

**National Committee for
Prevention of Child Abuse**

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NCPCA recognizes that there are many different and valid approaches to providing support systems for families. This booklet presents the views of the authors, who are experienced professionals with knowledge, expertise, and practical experience in the fields of child care, child abuse, and work with families.

The development and first printing of this booklet were made possible by a grant from the Skillman Foundation. NCPCA is particularly grateful to have the opportunity to introduce a publication on child care. The trend in the United States is toward both parents working outside the home, dramatically increasing the need for day care and thus heightening concern for exactly what goes on in day care settings.

Introduction

The purpose of this booklet is to make the reader aware of child care as a major resource for the prevention of child abuse as well as the special contribution that child care services can make to abused children and their families. It is hoped that this will bring people working in the two fields of child care and child abuse closer together. The discussion in this publication is intended to enhance communication and understanding between the two groups and to facilitate their working together for the benefit of children. It is hoped that the material presented will inspire the reader to take action. Wherever possible, the emphasis will be on specific actions, programs, and models.

Child abuse is a community problem, and its prevention is a community responsibility. The community must provide parents and children with certain supports, training, and information to help them cope successfully with their roles in the family. As part of a continuing effort to identify successful community approaches to child abuse prevention, the National Committee for Prevention of Child Abuse (NCPCA), in cooperation with the Johnson Foundation, convened two national research conferences on child abuse prevention in 1978 and 1981. Participants at these meetings, representing the many different disciplines and areas of expertise concerned with child abuse, analyzed what is known through research about preventing abuse. From their findings they identified community programs that, if they were available to all on a voluntary basis, would contribute to child abuse prevention.

While the experts seemed to agree that the earlier support can be provided the better, they acknowledged that for child abuse to be prevented, families need support at many different times. Thus, they identified programs directed toward each phase of the life cycle, beginning with the prenatal period and continuing through a child's school years. These programs include:

- Perinatal support programs – to prepare individuals for the job of parenting and to enhance parent-child bonding.
- Education for parents – to provide parents with information about child development and with skills in child care.
- Early and periodic childhood screening and treatment – to identify and deal with physical and developmental problems in children at an early age.
- Programs for abused children – to minimize the longer term effects on children who have been abused and to reduce the likelihood of their becoming abusive parents.

- Social skills training for children and young adults—to equip young people with the skills and knowledge necessary to succeed in adulthood.
- Mutual aid programs and neighborhood support groups—to reduce the social isolation so often associated with abuse.
- Family support services, including health care, family planning, child care, crisis care (such as hot-line counseling), marriage counseling, and related services—to provide families with the range of supports they need to survive the stresses of life and to stay together.
- Public information on child abuse—to heighten the public's awareness of different types of abuse and neglect and to provide specific information on how abuse can be prevented and where parents can turn for help.
- Community development activities—to increase local opportunities for job training, employment, access to social and health services, and other supports that reduce family stress.
- Communitywide child abuse prevention coordinating body—to guarantee that prevention programs are responsive to the needs of the community and to determine priorities for proposed programs.
- Child abuse prevention training—to give professionals and volunteers greater knowledge of the dynamics of abuse and to furnish them with information on community prevention programs.
- Ongoing program evaluation and assessment—to assure that community programs are as responsive and effective as possible.

Taken together, these programs comprise a comprehensive community approach to prevention as described in the NCPCA publication *An Approach to Preventing Child Abuse*. To encourage and assist community leaders in their efforts to prevent abuse, NCPCA is publishing a series of booklets describing aspects of the above programs and community activities. This booklet describes how adequate, comprehensive, and quality child care programs can significantly contribute to the prevention of child abuse and the enhancement of family life.

Child Abuse

Child abuse may be defined as any interaction between a caregiver and a child resulting in nonaccidental harm to the child's physical or developmental state. This definition includes physical and emotional abuse, neglect, exploitation, and sexual misuse. (While this definition is useful for the purposes of this booklet, it should be noted that the legal definition of what constitutes child abuse is determined by state laws.) The National Center on Child Abuse and Neglect in Washington, D.C., estimates the number of children abused annually in the United States at one million. The center also estimates the number of children who die each year as a result at one thousand. The center is quick to point out, however, that the estimate of deaths is low, because many child abuse situations go unreported or pass for accidents, to say nothing about the number of children reported missing each year.

The current approach to the problem of child abuse accepts the idea that 90 per cent of abusive parents are normal, feeling human beings. Only a very small percentage can be considered cruel, inhuman, or deranged or are severe substance abusers. Most child abuse situations are symptomatic of family stress or dysfunction and are amenable to treatment. Current research characterizes many abusive parents as social isolates with low self-image, often abused and neglected in their own childhood, often lacking an adequate parent model, and looking to their children for the love and attention denied them by their own parents. The parents usually characterize their child as "special" or wanted but often think of the child as "different." This difference may be real, as in the case of the developmentally slow child, or the difference may be imaginary. In either case, the "target" child becomes the scapegoat in the family.

Sometimes stressful changes in families, such as unemployment and divorce, may lead to child abuse. Given the proper conditions, anyone, regardless of class or cultural group, has the potential to become an abuser. Stress increases the possibility that parents will lose self-control. This stress may result from interpersonal problems, ill health, or financial difficulties.

The seeds of abuse may be sown very early, if parent and infant fail to develop close bonds. Attachment is an important ingredient in the development of a healthy parent-child relationship.

There are three victims of child abuse—the child, the parent, and the community. Taking this into account, society's response is directed not at punishing the abuser but at protecting the child and treating the family. There are laws against child abuse in all 50 states, and most of these laws require caregivers, including people involved in child care services and schools, to report suspected abuse. The laws also grant the reporter immunity from civil suit. Many caregivers and teachers hesitate to get involved, however, for belief in the privacy of the family is deeply rooted.

Parents are not alone in abusing children. Relatives, friends of the family, aberrant or sick members of the community, and society itself may commit the abuse. Examples of societal or institutional abuse include the abuse of children by prostitution and exploitation for pornographic purposes. Another example is the abuse that occurs in institutions supposedly set up for the benefit and protection of children. Harsh, punitive schools, abusive foster homes, unresponsive legal and judicial services, and institutions where children are "warehoused" are themselves abusive. A chaotic, unstimulating, or unduly harsh and regimented child care situation may be abusive. In addition, children in these settings often develop inappropriate coping skills that make them more vulnerable to abuse at home.

Update on the Family

No one would disagree that without children the human race has no future. Without adult care children cannot survive, and without youngsters to grow into adulthood, society cannot survive. The care of children is therefore one of society's primary concerns.

Society carries out its collective responsibility for the future through individual families. The family is the unit through which one generation brings forth the next and raises it to maturity. Family groups may not be the only way to rear children, but they do seem to be well suited to delivering the prolonged care and intimacy needed by infants. Certainly Americans are committed to the notion that the best way to rear children is within the family.

The family also has another unique function, one that sometimes comes in conflict with society's desire to ensure effective child rearing; it provides intimacy, love, and security to its members. It is the one place where individuals can in privacy truly relax, be accepted, and receive support.

Difficulty arises, then, when societal intervention in child rearing is required. This intervention may interfere with the privacy that families feel they are entitled to and require. The constant dilemma facing policymakers is how to maintain a good balance between the protection of children and the privacy of the family. Today the debate rages over children's rights vs. government interference in the family.

Historical Perspectives

The dilemma has been handled in various ways. The earliest societal interference in child rearing was simply to guarantee the survival of children. This included care for orphans and the abandoned and prevention of the worst abuses by parents. In the early days in the United States, on the other hand, the church established very rigid laws affecting all aspects of family functioning. After a relatively short time, however, the needs of the developing society and of individuals conflicted with the established regulations, and the laws were either changed or abandoned.

Later, when the needs of a developing industrial economy and the expansion of democracy required an educated population, free, compulsory education was introduced. This certainly interfered with the rights of families to determine how their children would spend their time and what they would learn. It also drastically affected the children's ability to contribute to the family income. Another example of intervention was the passage of child labor laws, which prohibited children under a certain age from working. During the twentieth century, regulations were introduced that required immunizations unless they interfered with religious beliefs. With some variation from state to state, government bodies established health and safety regulations and licensing of facilities occupied by children. All of these laws certainly constituted intervention in child rearing and in family functioning, but the greater need of society to protect children overruled the privacy of the family.

Currently, because of the rapid changes that are taking place, there is great concern about family policy. Some fear that the family itself is endangered. Others wish to reduce any interference by society in the family and in child rearing.

First, let's look at the changes that are taking place in the American family. It may be helpful to look at some of the historical material on the family and to recognize that change does not necessarily mean destruction.

The American Family Today

In *Here to Stay*[1], Mary Jo Bane surveys the development of the American family. She points out that because death rates of young parents in the past were almost as high as present divorce rates, even with the rise in divorce, more children today are living with at least one parent than ever before. As a result, there are fewer children in institutions, in orphanages, or living with relatives than in the past. Also, the rate of remarriage is comparable to the divorce rate, indicating that it is not marriage that is being rejected but a specific marital partner.

The 1980 census figures indicate that despite all the trends toward divorce and looser family arrangements, a family headed by a married couple is still the primary living arrangement for Americans, and by a very large margin. In 1980 almost 74 per cent of the population in the United States lived in a family headed by a married couple.

At present a major concern about the family is the effect on children of mothers working outside the home.* A prevalent myth is that in the past *all* mothers stayed home and reared their children. The facts are that a large majority of black women, both during slavery and after, have always worked outside the home, and immigrant women worked as servants, cared for the children of the rich, or worked in factories or in the fields. Only in the relatively short period from the end of World War I through the 1960s were large numbers of women at home and the main caregivers of their own children.

Whether a mother is at home or in the workplace may make less difference than is generally supposed. Studies show that the difference in the amount of time working and nonworking mothers spend with their children is surprisingly small. Bane indicates that television has become a significant rearer of children.

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* The authors of this booklet recognize that child rearing is the equal responsibility of both parents. If, as in this section, the burden seems to fall on the mother to be home with her children, this is because the attitudes and opinions of others are being reported.

It appears that although marriage and the family have undergone change, they are in no danger of disappearing. Similarly, those who fear that child care will change the family and eventually destroy it have unfounded fears. It is the authors' belief, as will be developed in this booklet, that providing supports to families, in particular child care, will strengthen, not weaken, the family.

Child Care Needs of Today's Families

Demographic studies indicate that the trend of mothers working outside the home will not only continue but will increase over the next decade. Caring for the children, therefore, will require assistance from outside the family. Rather than viewing child care as an intrusion into the family, child care can and must be viewed as a support for the family. Only by vast expansion of every type of child care service will the needs of families be met and the care for America's children be secured.

There are many alternative ways of taking care of children of working parents. Some businesses, for example, are turning to "flex time," which includes part-time work, different shifts, sharing of one position by two employees, and other approaches, generally geared toward female employees.

These innovative approaches are generally needed by families for the first few years of their child's life. It is urgent that more of these arrangements be available for parents who need to work for economic and career reasons.

Child care arrangements and facilities that reflect the various cultural and ethnic groups also need to be available. Children fare best when there is little discrepancy between the child-rearing practices of the parents and the caregiver. Parents are also more comfortable in discussing their children and communicating with people whose approaches to caring for children are similar to their own.

When parents need help in caring for their children because of work or for respite and they are unable to make satisfactory arrangements, great stress can result. Stress can cause problems in parent-child interactions, affect the parents' ability to work, and cause many health problems. Therefore, not only can adequate child care provide crisis intervention and treatment to alleviate the effects of child abuse, but it must be seen as a critical aspect of the prevention of abuse.

Case Study

The following case study illustrates how parents and day care staff can work together to the benefit of all concerned.

Mr. and Mrs. T.

Tanya T. is an attractive, intense woman in her late 30's who is sure of her priorities but finds it difficult to balance the conflict between working and parenting. Her professional life has been one of fighting her way up the executive ladder to a top administrative job. Her work is stressful but has many financial and psychological rewards. Tanya's husband, Tom, is a handsome sports enthusiast. They have two children, age 16 months and 3 years.

Their two girls are enrolled in an employer-sponsored day care center where they spend 10 hours a day. Soon after the children entered the program, the director of the center noted a problem. At times of great stress at their mother's workplace or when things were not going well at home, the girls would show signs of being overtired, irritable, angry, and generally in need of a good deal of reassurance, extra cuddling, and individual attention. During these periods the children, who were ordinarily dressed in the latest toddler fashions, would be brought to the center in their night clothes, without breakfast, and would have great difficulty separating from their mother. The director also noted that a crisis would occur whenever either or both of the children became ill. The parents were in conflict over who was to stay at home with the girls and who was to take them to the pediatrician. Tanya felt that she couldn't, and Tom either felt the same or felt humiliated because he was relegated to being a baby-sitter. This often resulted in giving the children some aspirin and taking them to the day care center with the hope that the symptoms would disappear or not be noticed.

Soon after the children were admitted to the program, a parent conference was held. The day care center staff felt a need to know what was going on at home in order to plan an appropriate program for the children. The director explained to Mr. and Mrs. T. that the center respected home routines and parental values and for this reason needed to know more about the family.

Tanya and Tom were defensive at first and claimed nothing was wrong. They complained that the children were being spoiled in day care and needed more structure and discipline. They described how the girls had been wonderful, docile children before *entering day care and how irritating and demanding they had become. In discussing these changes, a disagreement in child-rearing approaches surfaced. From this meeting and subsequent ones, it emerged that Tanya and Tom loved their children and were exemplary parents in many ways. They were capable of being sensitive to the developmental needs of their children and of providing a loving, secure setting for the girls. When times were stressful, however, and the requirements of the job and the marriage were overwhelming, the needs of the children were neglected.*

From these conferences, a plan was developed that acknowledged the needs of both parents and the children. On particularly difficult days, the children were to be brought to the center early, appropriately dressed. Their parents were to provide fresh fruit, and the center would provide cereal and milk for the children's breakfast. To increase their interaction with the center, Tanya and Tom were invited to have lunch at the center with their children. Arrangements were to be made at least an hour ahead of time in order to prepare the children and the staff for the visit. Telephone communication between the center staff and the parents was encouraged. On days when Tanya felt she had to meet with her colleagues for an after-work drink, the staff was to be notified so that the children would not be left waiting for her. Tom and Tanya were asked to take on some responsibilities in the center that matched their talents. Tom helped with some needed repairs, and Tanya helped to develop an improved collection process.

Soon after this mutually acceptable plan was put in operation, the center staff noted remarkable improvement in the children's behavior. Follow-up sessions with their parents also revealed favorable changes in parent-parent and parent-child interactions at home, due apparently to a healthy and helpful child care program.

Child Care

Child care can be defined as the shared care of a child by a caregiver and a parent inside or outside the child's own home for less than 24 hours a day. Views of child care have changed dramatically over the past decades. As families with both parents employed increase in all socioeconomic brackets, child care issues have changed from an emphasis on welfare and helping the needy to the provision of affordable, quality care for children.

History of Child Care in the United States

In the not so distant past, child care was a response to a societal crisis. For example, during the Civil War more men were killed than in any other war in which the United States has been involved, resulting in many fatherless families. Rather than placing children in orphanages or institutions for the insane or shipping them off to farms, the "day nursery" was developed so that mothers could work and still keep custody of their children.

In the early 1900s, day nurseries were provided for the "deserving poor" by charitable organizations. The "ladies bountiful" arranged day care for children of immigrants and the needy as a method of acculturating the children into the American way of life. These nurseries put a good deal of emphasis on cleanliness, godliness, and hard work.

With the advent of the depression of the 1930s, day care mushroomed in response to unemployment. Teachers, social workers, nurses, and nutritionists were put to work in WPA (Works Progress Administration) nursery schools throughout the country. This was followed by Lanham Act Day Care Centers, established during World War II to encourage women to work in defense-related industry. Although Congressman Lanham anticipated that the federally funded centers that bore his name would cease to be needed at the end of the war, in fact many women did not return to the home but became a permanent part of the labor force. Despite this fact, all federal funds for the centers were withdrawn, and in only a few areas were the child care programs supported by state and private funds.

Types of Child Care

According to some recent estimates, in the United States there are 6.4 million children under six years of age whose mothers work outside the home. This number is expected to increase to 10.4 million by 1990. In addition, there are at least 14 million school-aged children whose mothers work outside the home, and half of these children need care before and after school. Despite this increased demand for child care, there are fewer licensed day care openings now than were available in 1945.

In the recent past, the idealized concept of the American family included an at-home mother caring for her children. Day care was considered to be a temporary remedy until the mother could return to the home and assume her "rightful" role of caregiver and nurturer.

Although this attitude still exists, economic necessity and the feminist movement have made more people aware of the right of women to choose their career and to decide whether to work inside or outside the home.

In-Home Care. Say "child care" and most people picture a building with a sign that says "The ABC Child Care Program" or "The Jack and Jill Nursery School." Yet, among the various types of child care available, such centers provide the fewest openings for the millions of children needing care.

There are basically two categories of care for children: inside the child's home and outside the home. According to U.S. Department of Labor statistics on children five years old and younger, 31.6 per cent were cared for in their own home either by relatives (21.9 per cent) or nonrelated babysitters (8.7 per cent). The children who were cared for outside their home were enrolled either in family day care homes (38.2 per cent) or child care centers (20.2 per cent). The remaining 10 per cent were cared for by the mother at the workplace or in other arrangements not specified.

Little is known about care within the child's own home, because investigation into private homes is obviously limited to preserve the family's privacy. There are both advantages and disadvantages to in-home care, the most frequently used arrangement. It is probably the easiest, least expensive, and most flexible arrangement. Children need not be transported to another place, the surroundings are secure and familiar, siblings can stay together, and parents can maintain some control over activities, values, child-rearing patterns, foods, and schedules. There is no problem when children become ill. On the other hand, this is the least stable form of care, especially if the caregiver is unrelated to the family. In-home baby-sitters are usually not trained and have little or no access to training opportunities and support services, and they change jobs frequently because of low pay.

Out-of-Home Care. The least understood form of child care is called family day care. More than 35 per cent of all children in out-of-home care are in family day care, in which the provider is a neighbor, a relative, or a friend who cares for children in her own home for fewer than 24 hours per day. Family day care is an informal neighborhood system that provides support for increasing numbers of parents and children.

The number of children in a family day care home may vary depending on local restrictions, licensing laws, the space in the home, and the ages of children cared for. There are generally two types of homes: the small home operated alone by the provider who cares for fewer than 6 children; and the large group home, where the provider cares for 6 to 12 children with the assistance of another adult.

A few subsidized family day care networks have been developed recently that include both large and small homes. These systems provide assistance to the providers and parents in terms of training, paperwork, support services, and ongoing supervision.

There are many advantages to family day care. It is usually located near the consumer family, and the user and provider may share values and child-rearing practices. The hours may be more flexible than a center's. Because small groups of children are involved, the setting is usually intimate and paced. Cross-age grouping permits siblings to be together. Family care is often less expensive than center care, although this is changing. Unlike other forms of day care, family care will accept infants, non-toilet-trained toddlers, and mildly ill children.

The disadvantages to family day care include the lack of stability among providers, the dependence on one person to meet the needs of a number of children, and the lack of a back-up when the provider is ill or on vacation.

Another consideration is that family day care is by and large unregulated. Usually the only time family day care comes under scrutiny is after a report of child abuse or neglect. Licensing of family day care homes is very difficult and expensive, so in effect parents are the primary licensers of this type of day care.

Day Care Centers. Day care centers come in many forms, shapes, and sizes. They may be sponsored by a community group, school district, church, or temple. They may be privately owned and operated for profit; they may be part of a national corporation; they may be run by unions for their members; they may be connected with a university, college, or hospital; or they may be operated by industries for their employees. A center may care for anywhere from 15 to 300 children. The physical facility may be anything from a storefront to a laboratory school built especially for children. A program may be totally or partially subsidized by the government, charity, or business, or it may be totally self-sufficient and dependent on parent fees. According to Allison Clarke-Stewart, professor of social ecology at the University of California at Irvine, children "are usually divided into classes according to their age. The average class size is ten for infants and toddlers, seventeen for three-year-olds, nineteen for four-year-olds, and twenty for five-year-olds. Most children in day care centers are three- or four-year-olds. Teachers in the centers tend to be young and of the same race as the children."[2]

Day care centers are attractive to parents because they often offer more structured programs that parents believe are educational. Centers are also more likely to be licensed and monitored for health and safety requirements. In addition, stability is not a problem. Although the staff may change frequently (usually due to low pay), the center remains. If one staff member becomes ill, there is another to care for the children. Hours, tuition, and rules are predictable. This is an advantage to some parents, while other parents need more flexibility in order to meet the needs of their situations. Centers will not accept sick children, but preventative health care and nutrition may be provided. There is always more than one adult at a center, giving parents and children opportunities for varied contact.

Finding Child Care Services

Finding an adequate, stable child care arrangement can be one of the most stressful situations a parent faces, but the benefits can be enormous. Making a good match in child care between a caregiver and a family can dramatically improve the parents' chances of being effective workers, parents, lovers, and friends and thus minimize opportunities for abuse and neglect.

The particular type of child care preferred depends on the age of the children, past experience of the parents, location, financial considerations, expectations, and ethnicity. In Richard Ruopp's National Day Care Study, published by the U.S. Department of Health and Human Services in 1979, respondents preferred care in the child's own home for children under one year of age, family day care for children from one to three years of age, and a more structured arrangement such as center care for children three and older. Ethnic differences surfaced in this study, with the black families interviewed showing a strong preference for center care.

Studies have found that parents want child care that is (1) affordable, (2) located near their home, (3) available at convenient hours, and (4) the "right kind with respect to sponsorship, facilities, program, and personnel."

Unfortunately, even when child care that suits a parent's preferences is available, parents often have difficulty finding it. Some find child care through newspaper ads or the yellow pages of the phone book. Another source is signs posted in laundromats or local stores, but most arrangements are made by word of mouth. Pediatricians are among those most depended upon to help make good child care arrangements, but they may know little more than the parent in terms of what is beyond the immediate neighborhood. The distraught parent may take the first arrangement that turns up, while there may be a more suitable arrangement one block away. Sometimes parents simply don't have or don't take the time to find the best place for their child. More often, however, parents haven't the slightest notion of how to find that place.

In the past 10 years, information and referral programs have sprung up to fulfill this great need of bringing caregivers, centers, and parents together. These programs survey the neighborhoods they serve and locate available child care places. When parents contact the information and referral agencies, three or four names of possible spaces are given, based on the family's needs. Obviously, such systems can be only as good as the child care available in the areas they serve; even the best referral system can't be of much help in locations where there are few or no openings for children.

Quality Child Care

Quality child care is of course what every parent and professional wants, but its definition varies, depending on one's philosophy of child rearing. Obviously any definition of quality includes a healthy and safe environment; adequate and age-appropriate toys, equipment, and programming; and adults who are interested in their work. Ruopp's National Day Care Study reported that quality in preschool center programs had a good deal to do with the composition of the day care classroom, including the ratio of caregivers to children. "Smaller groups of children and, to a lesser extent, higher caregiver/child ratios (fewer children per caregiver) are associated with more desirable behavior and higher test score gains. Moreover, aspects of caregiver qualifications, especially education/training relevant to young children, are associated with positive classroom behaviors and superior test score gains."

All studies indicate that the key to quality lies in the match between the caregiver, the child, and the family. All the most wonderful equipment, nutritious meals, and stimulating programs will not provide a quality child care arrangement if the family's values conflict with those of the caregiver. So the issue of quality often hinges on how discipline and punishment are handled, how separation is worked through, how routines such as toilet training, weaning, feeding, and napping are viewed. Many children spend most of their waking hours in child care arrangements, and no matter how attractive the program looks, there must not be too much discontinuity between the caregiver and the parents.

This raises the issue of how child care providers can deal with an abusive or neglecting family. In these situations the staff can serve the child and family by providing the best possible care for the child while respecting individual differences and values. For example, if a parent offers permission to the caregiver to spank the child, the caregiver can discuss alternative methods of discipline, explaining that spanking is against the rules and not the most effective way of achieving the kind of behavior desired by both parents and caregiver.

Attachment

Many people, including some well-known experts, have reservations about day care for very young children. They worry that separating the baby from his or her parents at a time when infant bonding and attachment should be developing will prevent or delay the attachment process. Recent research, however, indicates that healthy parent-child attachment can occur when even very young children are placed in an appropriate day care setting. Other studies have explored the possibility that close relationships with caregivers might alienate infants and children from their parents. These studies demonstrate clearly that children prefer their parents over their day caregivers, when they are offered a choice in a stressful situation. Providing a warm, loving caregiver for an abused child actually often results in an improved parent-child relationship. Child care can provide essential respite for parents.

Latchkey Children

Another important aspect of the child care issue is the problem of latchkey children, children who take care of themselves for varying portions of the day or night. The sheer numbers of unattended children involved would make this an important issue under any circumstances, but it is made all the more important by the fact that so many communities are not safe places for children. Drugs, violence, thefts, and emotionally disturbed adults are all too much a part of the current scene in many communities. A recent study by Thomas Long, Ed.D., in the School of Education at Catholic University in Washington, D.C., has documented the wide extent of the situation and the significant effects on the latchkey children. Most of the effects are negative, such as boredom, loneliness, and fear, but latchkey children also derive benefits from their situation in terms of increased self-reliance, responsibility, and pride. Survival courses and kits for children and parents are being developed by community groups such as the Boy Scouts, the Girl Scouts, the Camp Fire Girls, YMCAs, and 4-H Clubs. The Kansas Chapter of the National Committee for Prevention of Child Abuse has developed a program called "I'm in Charge." Part of the program is a film entitled *Lord of the Locks,* which dramatizes important lessons for latchkey children.*

After-school programs are being developed in a number of communities across the country. One recommendation has been to have the public library, the recreation department, and the public school in a community team up to plan and implement an imaginative program. Parents in many communities across the United States have developed informal arrangements in their own neighborhoods to meet the after-school care-giving problem. Parents take turns caring for all the children on the block, or one parent or more agrees to fill this role for all the families in a neighborhood, either on a volunteer basis or for a fee. Many other imaginative after-school programs have been developed by groups of parents.

Baby-sitting

Baby-sitter is defined in Funk and Wagnall's Dictionary as "a person employed to take care of young children while the parents are absent." With the decline of the extended family, the practice of employing baby-sitters has become widespread. In the past the role of baby-sitter was filled by grandparents and others living in the home. Today this situation seldom exists, so the parents often turn to people outside the family.

Older children are also often used as sitters for their younger siblings. In some cultures a large measure of the responsibility for child care is taken over by the older children in the family. In the United States there are undoubtedly many 12- and 13-year-olds who are capable of baby-sitting. In general, however, school-aged children do not have the knowledge or mature adjustment to be given the full responsibility for child care. Also, shouldering this burden in some cases robs children of important childhood experiences.

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* Further information about the program can be obtained from the Kansas Chapter of NCPCA at 435 S. Kansas, 2nd Floor, Topeka, KS 66603, (913) 354-7738.

The danger of using untrained and inappropriate baby-sitters because of the potential for accidents and child abuse has been recognized only recently. Many pediatricians and other health professionals working with families place this issue high on their list of subjects to be discussed with parents. In some communities the Red Cross, the schools, and youth-serving agencies such as the Girl Scouts, the Boy Scouts, and the Camp Fire Girls have organized classes to improve the quality of baby-sitting among teenagers.

Parents should exercise care in choosing baby-sitters. Once selected, the sitter should be given instructions regarding activities with the child and disciplining the child. The sitter's behavior should also be clearly circumscribed. Drinking, smoking, using drugs, using the telephone to talk to friends, entertaining, and other potentially dangerous activities should be forbidden. It is also important for the sitter to have *in writing* the telephone number where the parents or some other responsible adult can be reached as well as emergency numbers for the police, paramedics, and fire department.

It would be wonderful if all parents knew where to obtain baby-sitting services. This would minimize the possibility that children would be left alone or left in the care of inappropriate or incompetent adults or children. Every community and neighborhood should have a pool of reliable, experienced baby-sitters. Alternatively, friends or neighbors could band together to exchange baby-sitting services. Helping to develop such an arrangement or pool or hot line could be an exciting and worthwhile project for a group of community volunteers.

Handicapped Children[3]

There are many working families that require before and after school care, night care, weekend care, and respite care. Similarly, there are families that require care for children who have needs different from the needs of their contemporaries. Day care should be structured to meet the needs of all families, including those with children who have special needs. These children are at higher risk for abuse, and child care can be important to the prevention of such abuse. An example of a program that meets the needs of such parents is Project ABC (Any Baby Can), which links children with special needs to appropriate services at the earliest age possible.*

Services for children with developmental and physical handicaps are rapidly changing as educational, health, therapeutic, and social agencies adopt programs to meet the mandates of Public Law 94-142 (Education for All Handicapped Children Act) and other federal and state laws. These laws promote the inclusion of all children in programs that meet their developmental needs regardless of their handicaps or medical records.

Parents can be helped greatly to accept their child's disability in a supportive setting where concerns and common problems can be shared among parents during visits, conferences, and parent get-togethers. No one can argue against the positive effects of providing a warm, loving, communicating environment for children experiencing mental, sensory, motor, or emotional handicaps or children with health impairments. Day care can provide for the majority of needs for the handicapped child under 24 months of age, although some children, such as the deaf child, may require special activities to meet specific needs, and appropriate consultation should be sought.

As the handicapped child grows older, specific interventions beyond the capability of conventional child care programs may be required. The child care staff, working with appropriate consultants, can devise mechanisms to ensure that all children are appropriately assessed to detect delays in communication and in social, motor, and affective skills. If atypical patterns are detected or suspected, consultation should be sought with health and educational professionals skilled not only in diagnosis but also in assessing functional abilities and developing appropriate intervention plans and services.

As the child increases in age, the specialized needs of the child often become more pronounced. Day care programs must establish a policy in consultation with parents and health and educational personnel regarding the program's ability to meet individual needs. For school-age children the educational and therapeutic needs of the child most frequently are met by the public schools, and the child care center provides the before and after school supervision required by working parents. Most schools are implementing mainstreaming programs, and mainstreamed handicapped children may function very well in day care programs along with nonhandicapped children.

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*Further information about Project ABC can be obtained from the San Antonio Chapter of NCPCA, 1011 W. Woodlawn, San Antonio, TX 78201, (512) 732-1051

The majority of children with mild handicaps are not identified by age 24 or 36 months. These include children with mild mental retardation, mild-to-moderate speech and language disorders, and learning disabilities. These children are best served in settings that enhance their total development; day care programs of high quality provide such settings. Severely handicapped children, on the other hand, may require more specialized day care that can be provided only by a trained family day care provider or in a special day care center.

An often neglected aspect of day care is respite care—the service provided a family on a short-term basis to allow a parent a few hours of relief from the care of a severely handicapped child. A very young child generally poses few problems during such respite care periods, but the older, ambulatory child may need more specialized care and supervision. Each program must carefully evaluate its ability to provide high quality care for these children with special needs.

It is universally recognized that handicapped children of all ages are at greater risk for abuse. Caring for a child with special needs creates great stress in families, and child care, both respite and ongoing, has been shown to be one of the best approaches to preventing such child abuse and neglect.

Crisis Child Care

Another form of child care is the crisis nursery or the crisis child care center. These are centers to which parents who feel overwhelming emotional stress or pressure can bring their children until they are able to cope. This gives parents the opportunity to express their anger and frustration appropriately and to pull themselves together rather than exploding and taking their feelings out on their children.

The first crisis center was established in Denver, Colorado, in 1973 as part of an overall child abuse prevention package. The center has remained an integral part of this pioneer program. Since 1973 many crisis centers have sprung up across the country, such as the El Paso Crisis Nursery in Texas. Some centers provide minimal services, their main purpose being to provide time away from their children for harried parents. Others provide broader services for both parent and child. All can be truly effective only if they are open around the clock and if they establish appropriate ties with other community services. For these reasons, an established child care facility, especially one associated with a 24-hour institution such as a medical center, might have the best potential for developing a crisis child care center.

Therapeutic Child Care

Group care of children can be organized to provide a therapeutic milieu for children. This kind of undertaking requires that the caregivers either be skilled mental health professionals or work under the direct supervision of such professionals. In the past, this kind of therapy was usually reserved for emotionally disturbed children. In recent years, however, centers working with abused and neglected youngsters have used this approach with some success. The results seem to be dependent on the goals of the program, the kind and degree of inflicted trauma, the pathology in the family, the skill of the therapists, and many other factors. The goals of most programs include relieving anxiety and fear and instilling heightened self-esteem and improved self-image in the youngsters. The children are encouraged to express and share feelings, to learn appropriate coping skills, and to learn to avoid rather than invite abuse by adults. As prevention of further abuse is a major goal, concurrent parental counseling and appropriate parental involvement in the program are usually included in the therapeutic package. Therapeutic group experiences appear to be especially effective with children who have been sexually abused.

The Financial Dilemma of Child Care

According to the Canadian Council on Children and Youth, "The customary conditions for a stable family and community environment no longer exist for increasing numbers of young families. If we accept that successful child rearing is crucial to the establishment of a stable society, we must be prepared to supplement the efforts of individual families in carrying out this responsibility.

"To this end, we must reject the concept of day care as a baby-sitting service for working mothers or, worse, as a remedial service for inadequate parents. Day care services must be perceived as supports and enrichments to family life in general which offer the young child essential opportunities for socialization."[4]

A good child care center will use from 80 per cent to 90 per cent of its budget on salaries for the caregivers. This is to ensure that there are enough adults to attend to the individual needs of children. In most cases, unfortunately, these teachers and aides receive low wages. Yet, if child care salaries were to be increased, most working class families, unable to qualify for state support, could not afford child care.

Those families that are unable to purchase or find good child care may, in the long run, cost society much more than it would have cost to provide good child care. It is cheaper to put resources into early preventative programs (in this case child care) than to spend dollars later for remediation and intervention. A recent longitudinal study has demonstrated this. The Perry Preschool Project demonstrated that for every $1,000 invested in the preschool (child care) program, at least $4,130 (after inflation) will be returned to society in the form of reduced costs for education and legal processing for delinquent behavior and increased life-time earnings for participants.[5]

Child care programs face a mighty dilemma, summarized in the following statements:

- Children must have good child care in order to learn and grow and minimize the need for later, costly intervention;
- In order to provide good child care there must be enough caring adults who receive adequate salaries; and
- In order for working parents to pay the full cost of care, child care must be affordable.

To resolve this dilemma, a national child care policy must be developed that will address this crucial issue.

Case Study

The following case study demonstrates the mutual benefits to society and the family of appropriate child care.

Mabel B.

Mabel B. is a single parent who came from a very disturbed family background. Her father was an alcoholic who became violent when under the influence and could never hold a job. Her mother, after being battered by her husband, would often take out her rage and frustration on her children. Mabel was a frequent target and remembers wearing long-sleeved shirts and jeans to school to hide the bruises.

Mabel married a man very similar to her father. After five stormy years, she divorced him and went on welfare to support her three children. She describes a feeling of numbness as she staggered through the next few years. Finally, with boys then six and eight in school and her three-year-old daughter toilet trained and ready for *preschool, she decided to enroll in an LVN (licensed vocational nurse) training program. Her plan was to put her daughter, Susan, in a day care center and her sons in an after-school program, but she could not find any affordable child care services in her neighborhood. Reluctantly, she asked her mother to help out. The children's grandmother agreed to baby-sit all the children while Mabel was in school.*

A few months later Susan was admitted to Children's Hospital with second-degree burns on her buttocks. The medical staff suspected that the burns were nonaccidental and reported this to the hospital social worker and child abuse team who, in turn, reported to child protective services. When Mabel and her mother gave a series of conflicting, changing, and impossible explanations for the burns, the child abuse unit of the local police was called. Mabel then gave the officer and the protective services worker a more plausible explanation. Mabel stated that her mother had been playing "chicken" with the youngster. She would hold her over a pot of boiling water on the stove, telling the child that chickens get cooked. The juvenile court ruled that the grandmother's actions were "child endangering," and Mabel was prohibited from leaving the children with her. This came at a time when Mabel was close to completing her training and reaching her goal of independence. An adequate child care plan was essential for her.

At this point the protective services worker stepped in. She knew that abused and neglected children had first priority for service in subsidized child care. She called an appropriate child care center and made the referral. Despite the center's long waiting list, places were found for Mabel's youngsters. Mabel was able to complete her training and subsequently found a position as an LVN at a local hospital. She is off welfare, and Susan and her brothers are thriving in a safe, nurturing, developmentally appropriate environment.

Child Care and Child Abuse Prevention

What is the relationship between child care and child abuse prevention? The role of child care in child abuse prevention is to support the parents in doing a quality job of parenting. The quality of parenting is determined partly by how well prepared parents are for their role, partly by how parents themselves were parented, and partly by current family interactions. Mothers and fathers who feel good about their own childhood, have a positive model to work from, and have a healthy self-image are likely to do well. This is especially true if they feel supported and appreciated within their family group and community. Without jobs, decent income, housing, health care, and other support systems, even the best prepared, best oriented fathers and mothers may find their task intolerable, and some form of child abuse may result.

All families require some form of ancillary child care services at some time, and many families need child care services on an ongoing basis. In today's world more affluent families use housekeepers, baby-sitters, nursery schools, after-school programs, and activities such as music lessons, dancing, and camps as support services. The less affluent and the poor use relatives, neighbors, siblings, and, when available, community services.

All children, at some times in their lives, can benefit from children- and youth-oriented services that go beyond the care provided by even the best of parents in the best of circumstances. The development and stimulation offered by appropriate out-of-home child care experiences as well as the opportunities to interact with other children and adults can be very valuable.

Mothers and fathers need assurance that their children are safe and well cared for while the parents are at work or away from home. This assurance is important to relieve parental worry, guilt, and feelings of loss when separated from the children. For many parents, knowing that the children are in good hands enables them to pursue their job or career and outside interests, resulting in an improvement in mental health and a lowering of family stress. Without such time away from child care responsibilities, many parents become tense, anxious, and depressed. In this state of mind they are less able to cope with the stresses of child rearing. This may result in a lowering of self-control, which places the children at risk for abuse. This is especially true for parents who were abused as children.

National Committee for Prevention of Child Abuse

Abusive parents and families are often very isolated. They often have no relationships with anyone in their community, even their next-door neighbors. Appropriate child care services can provide relief from this isolation. Involvement with their children's other caregivers may provide some parents with their only adult relationships other than those at work. Even brief contacts with a child care center director, teacher, or a family day care mother can be very supportive and provide some relief from isolation.

Adequately trained caregivers can also serve as teachers and role models for parents. They can help fathers and mothers to understand and accept normal child behavior. They can also help parents learn reasonable ways of coping with the stresses of child rearing. In many cases child abuse occurs because parents have unrealistic expectations of their children's capabilities. Caregivers can serve as role models for mothers and fathers who have experienced poor or inadequate parenting and therefore have no good role models, and this can be done without weakening parental authority or undermining parental ability to teach and model desirable cultural and family values.

Appropriate child care services can also improve the quality of life for children who, while not actually abused, live in a less than desirable family situation. This includes children who are well taken care of physically but who need to build self-esteem through positive contacts with peers and adults rather than demeaning, negative ones. The care, nurturing, and support of a warm, sensitive caregiver can be a new and constructive experience for these children and can serve as a model for their parents.

The child who is "different" in terms of development or behavior and the child who, for a variety of reasons, becomes the scapegoat in the family are both at high risk for abuse. Optimal child care outside the family setting gives these children an opportunity to enjoy an accepting, warm, nurturing environment, which they may not be experiencing at home. In addition, supportive child care services can give parents an opportunity to step back and examine their feelings and actions toward their "special" child. In an appropriate child care setting, such children also learn social and coping skills that will improve the situation at home. The abused child whose behavior tends to invite more abuse may learn from peers and caregivers how to change that behavior. Children can learn the negative consequences of their behavior and the rewards of more acceptable behavior. It is important for the child's parents to be involved in the therapeutic process. This can be achieved if there is a comfortable relationship between parent and caregiver.

Quality child care services, planned and implemented by caring, skilled, knowledgeable adults, can also provide the means to identify children and families at risk before physical and sexual abuse occurs. Caregivers can learn to recognize the signs of family dysfunction that can lead to physical and sexual abuse and can help children learn how to protect themselves. This early identification of a problem provides the opportunity to guide these families to appropriate community resources.

Conversely, parents should be on the lookout for signs of dysfunction in the child care setting, although most child abuse, including sexual abuse, does not occur in child care settings but rather in the home. Parents can protect their children from abuse in child care by maintaining communication with the caregivers, talking with other parents using the same facility, being suspicious of any limitation on parental visiting or being prohibited from seeing any room or area inside or outside the facility; and above all, by talking and listening to their children and noting any changes in their behavior. Direct parental involvement in a child care program is another safeguard. (See Appendix D for a list of safeguards.)

A number of programs have been developed to help caregivers, parents, teachers, and children cope with sexual misuse. The *Bubbylonian Encounter*, for example, is a child sexual abuse prevention play for school-aged children developed by the Kansas Chapter of the National Committee for Prevention of Child Abuse in conjunction with the Theatre for Young America and the Johnson County Mental Health Center. The production uses humor, drama, and audience participation to illustrate both positive and negative touching. Through the play's leading character, children learn what steps to take if forced touching should occur. Each performance also provides an opportunity for consultations between parents and professionals. Many educational models have been developed for children, parents, and day care providers (see Appendix A for one such model).

The children of parents who are physically, emotionally, or mentally handicapped are often at risk for emotional, if not physical, abuse. These families need help, including quality child care services that provide nurturing and growth-stimulating experiences for the children and supportive services for their parents.

When newborns leave the hospital for home, they disappear from community view until they enter school. This is a gap of about five years, and during this time families have no compulsory ties to the community, nor are they given support or guidance. Quality child care services, integrated into the neighborhood, could fill the gap. Such an arrangement would offer care to all children and their families. This would allow screening for difficulties such as abusive situations while promoting healthy child and family development.

Questions and Answers about Child Care

The following are questions parents frequently ask about child care.[6]

I feel so guilty about having someone else care for my child. Won't this separation interfere with my child's development and our relationship?
Available evidence indicates that the opposite is true. There are many books, papers, and manuals that support the idea that quality day care services usually enhance child maturation and development and may improve the parent-child relationship.

Is day care harmful to the physical health of my child?
Children in high quality day care compare very favorably with children reared in their own home in terms of physical health. The advantage of early detection and treatment of illness appears to far outweigh the slightly increased possibility of picking up mild infections such as colds and diarrhea. Also, a carefully planned nutrition program can not only improve the health of the child but also provide nutrition education for both the child and the family.

Is day care harmful to the mental and social development of my child?
Available evidence appears to indicate that children in child care compare very favorably developmentally with children who remain at home with their parents. The benefits of developing cognitive, affective, and social skills through interaction with other children and nonfamily adults in a safe, structured setting supervised by a caring, knowledgeable adult are far greater than the possibility that the child will miss some of the warmth and depth of the parent-child relationship.

Will my child love and respect the caregiver more than me?
There is abundant evidence that children in day care still look to their parents when there are decisions to be made and prefer their parents in times of stress. It is not the amount of time parent and child are together that establishes appropriate bonding and attachment but rather the quality, security, and predictability of that interaction.

National Committee for Prevention of Child Abuse

Will a child who attends a day care center or nursery school be bored when he or she goes to school?
All the evidence appears to show that this is not true. The gains children make in emotional, social, and cognitive well-being in quality developmental day care appear to improve their motivation for learning and hence their school performance.

Will the day care center or other caregiver handle my child differently than I do and make it difficult for me to rear my child the way I want to? In short, will my child be brainwashed and alienated from the family?
The best way to avoid this problem is for parents to be involved with their child's care and to communicate with the caregiver. If the differences are too great, a change of setting is advisable.

What to Do and How to Do It

Starting a Child Care Service

One of the advantages day care services provide for parents and children is the opportunity for them to interact with the community in which they live and an opportunity for the community to play a role in determining the quality of its citizens and its families in the next generation. In addition, the individual who chooses to become involved with starting a child care service has the opportunity to seek and find creative solutions for the benefit of children and to be involved with both families and the community as they evolve.

The person considering starting a child care service should have at least an elementary knowledge of the issues involved in child abuse prevention and optimal child care services. Having satisfied this prerequisite, the following actions should be taken:

- Survey the community for areas of greatest need. What are the gaps in service for children and families? Which children are most in need of child care? Which families are most in need of support services? What kind of child care services would relieve family stress for these families and meet the developmental needs of the children served?
- Survey the community for existing services, asking also about programs that started but failed. Which agencies, individuals, and programs could be helpful if a new child care service were to be established? Does the community have a Junior League, Council of Jewish Women, or chapters of other national groups that have shown interest in child abuse or child care?
- Look for and offer to work with any groups or committees that are attempting to coordinate services in that community, such as the United Way. How might a new service work into any existing network of social services? Is there an available information and referral service? Can a new service develop linkages with other family and children's services in the community such as social services, health services, child care services, business and industry, and legal and governmental services?
- Determine if a physical facility is available that will meet the needs of the children and also the local health and fire regulations and the state and local licensing codes. Could insurance be obtained for a child care service?
- Develop a board of directors or group of supportive individuals to work with and to enhance explorative and planning

strategies. If possible, this group should include people from different disciplines and different segments of the business and professional community. A group of five or six would be adequate in the early planning stages. Consult with professionals in the field and obtain appropriate literature regarding staffing a child care service. What child-to-staff ratio is appropriate for different ages of children? What level of training and experience is optimal for the kind of program being developed? What organizational structure will best accomplish the goals of this particular child care service?

- Explore funding possibilities, including available and potential sources of income. What would be an appropriate fee schedule? What private or governmental funding is available or potentially available? Could ties with existing agencies or groups be helpful?
- Think through the possibilities for evaluating the program. If the reduction of child abuse is a goal, what criterion could be used to judge success or failure? Which community agencies could contribute to the evaluation by providing data on the families served? If the development of coping skills in the children is a goal, what measures have other child care services, such as Head Start, used to evaluate their programs?
- Choose a competent child care professional to direct the program. It might be appropriate to choose this person early in the exploration process to share the burden with the program originator and the group of advisors. It is important to find a professional with whom the program originator can work comfortably on a day-to-day basis, even though they might not agree on every detail.

After examining the issues listed above, it may be determined that the establishment of a child care service is not possible or appropriate in this community at this time. If this is the case, an advocacy approach might be considered, if conditions in the community warrant it.

Child Advocacy

Children are powerless; they have no money and no vote. They are dependent on adults to meet their physical, psychological, and developmental needs. Governmental policies, however, place children on the lowest level of priority. During periods of lessened governmental resources, the greatest cuts in service are directed at programs that support families and children. Because children are the first to be hurt, children must have advocates.

A major role of child advocacy is to be involved in the legislative process. When bills are pending that would either benefit or harm children, support or opposition should be expressed to local and national legislators. Personal letters, letters from friends, and letters from members of organizations or churches are of key importance. Legislators respond to their constituents, and if enough voices are raised in favor of child protection, they will vote accordingly.

After pending legislation has been studied, the advocacy effort can be broadened by writing letters to the editors of local newspapers, giving talks to organizations that need and want more information, and organizing small groups of neighbors and friends who are interested in what is going on. It is important to use existing resources as much as possible. Determine which agencies, groups, or committees already active in the advocacy field would welcome support and active participation. Which others would supply advice and guidance? Appendix C lists organizations that could prove helpful.

Much child advocacy can be accomplished through an organization or church group that wants to become more involved with child care and child abuse prevention activities. A committee or a group within the organization could be instituted to increase expertise and activities in behalf of children. A number of child abuse prevention activities relating to child care could be explored by such a group, including a day care program or nursery school, an after-school or latchkey children's program, a day care information and referral service, a baby-sitting service, or a sexual abuse prevention program.

Volunteers

No discussion of child care would be complete without mentioning the role of volunteers. Because of the efforts of volunteers throughout the world many children are spared from exploitation, inequity, and injustice. In the fields of child abuse treatment and prevention and child care, there are many examples of outstanding contributions by individual volunteers and volunteer organizations.

Summary and Conclusions

Opponents of the expansion of day care and child care services argue that the American family is already being threatened by too much outside interference. They state that (1) day care is a threat to the American home and family by encouraging parents to abrogate their responsibilities; (2) day care allows psychologists, educators, and bureaucrats to brainwash children and to usurp the rights of parents and families; and (3) day care interferes with and weakens the normal relationship between parent and child.

Current research does not support these points. It has been found that children in quality day care compare very favorably in all spheres with children cared for in their own homes. Children in high quality day care show gains in cognitive, affective, and social development equal to or better than the gains of their peers cared for at home. The data also show no evidence of brainwashing, no interference in the parent-child relationship, no "invasion of privacy," and no undermining of home and family. On the contrary, there are indications that day care seems to support the home and the family and to minimize child abuse and neglect, especially when parental involvement in the day care setting is encouraged.

In the 1980s the United States has become increasingly aware of and concerned about the magnitude of the problem of child abuse and neglect. In developing a national policy to ameliorate this shameful problem, child care must be considered a vital resource for prevention and treatment. Exploration and support of a variety of child care models at the federal, state, and community levels are essential in order to assure available and appropriate resources for all families. The development of this kind of child care system would be a giant step in the direction of a society relatively free from child abuse and neglect.

Appendix A: A Day Care Model

A study group of the American Orthopsychiatric Association published a report on the mental health aspects of day care in 1973. This report is as valuable today as it was then and can serve as a model for standard setting and a guide for health and mental health professionals who wish to advocate for children through support day care.[7]

The report develops 18 issues, which are paraphrased as follows:

1. All aspects of the child's development should be considered in planning and evaluating a day care service.
2. The experiences planned for the child should be maximally suited to the child's individual developmental needs.
3. The day care program should encourage the child to explore, make choices, and develop a variety of coping methods.
4. The day care program should promote the expression of a balanced variety of feelings.
5. The total day care experience should enhance the child's task orientation.
6. The total day care experience should facilitate the psychological move between the family caretaking environment and the day care environment.
7. Day care services should supplement and complement the family rather than replace that basic caretaking unit.
8. In a given community, a family should have the true option of using family day care, group care, or some combination of arrangements.
9. Continuing professional help should be available to the family and should be defined by both the professionals and the family members.
10. The basic child-rearing pattern associated with certain ethnic and racial groupings should be fully recognized in organizing a particular day care service.
11. In planning help for the family, special attention should be given to family-child relationship experiences.
12. The day care program should include those experiences that are not available in the home and are felt to be critical to the development of the children being cared for.
13. A structure should be developed that ensures adequate day-to-day relevant communication between child care staff and parent.
14. One member of the caretaking staff should be fully informed about the total development of the child and family and should be the advocate of necessary changes to promote that development.
15. Administrative practices should support autonomy in decision-making on the part of staff responsible for children.
16. Staff working with children should receive stimulation and support from their administration.
17. Restriction of activity because of possible safety hazards should be carefully considered.
18. The size of the day care center should be kept small.

In their concluding remarks, the members of the study group recommended the following criteria for the evaluation of day care programs:

- Attention to individual needs.
- Attention to all areas of functioning.
- Promotion of the child's active choice-making.
- Encouragement of learning to deal with a variety of feelings.
- Enhancement of engagement as opposed to passive receiving.

The study group also suggested that a model program be based on the concept of the extended family, characterized by:

- Extensive communication with caregivers, being responsive to the needs of the family, and encouraging the participation of families.
- Support of family resources by both the caregiver and continuing, well-trained professional help.
- Supplementing of family-to-child experiences in the day care setting, especially in those critical areas where direct help to the family is not feasible.

Appendix B: Additional Reading

Child Abuse

Bourne, Richard, and Newberger, Eli, eds. *Critical Perspective on Child Abuse.* Lexington, Mass.: Lexington Books, 1979.

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Appendix C: Organizations

Local Community Resources

Within each community there are agencies and organizations that may be useful in helping to define the needs of children in the community. They may also be able to assist in establishing child care and child abuse prevention programs. The following list of agencies, organizations, and committees typically found in a community will give the reader an idea of the possibilities that may be available.

Governmental Agencies

- City or county community development divisions or committees
- City council
- County board of supervisors
- Social service or welfare department
  - Child welfare
  - Child protective services
  - Protective services
  - Child care licensing

Educational Programs

- Community colleges (individual departments such as education, home economics, early childhood, psychology)
- Universities (individual schools and departments)
- Adult education
- Parent-Teacher Association (P.T.A.)

Community Services

- United Way
- Welfare and Information Service
- Red Cross (babysitting training and child care classes)
- Family service agencies
- Religious organizations (churches, clubs)
- Information and referral programs (child care information and referral, parent education, child abuse prevention)
- Self-help groups (Parents Anonymous, Parents United)
- Salvation Army, Volunteers of America, and others
- Family crisis and stress centers

Youth Serving Organizations

- Boy Scouts, Girl Scouts, Camp Fire Girls, Woodcraft Rangers
- YMCA, YWCA
- 4-H Clubs

Women's Organizations

- League of Women Voters
- National Organization for Women (N.O.W.)
- Junior League
- American Association of University Women
- Council of Jewish Women
- Council of Black Women

Service Clubs

- Veterans' groups
- Lions, Rotary, Kiwanis, BPOE (Elks), Knights of Columbus, and others
- Chamber of Commerce and Junior Chamber of Commerce

Most of the organizations and agencies can be located in the telephone directory under their own names or under "Social Services," "Community Services," or "Information and Referral Services."

National Committee for Prevention of Child Abuse

National Child Abuse Organizations

American Humane Association
Children's Division
9725 E. Hampden Avenue
Denver, CO 80231

International Society for the
Prevention of Child Abuse
and Neglect
1205 Oneida Street
Denver, CO 80220

C. Henry Kempe National Center
for the Prevention and
Treatment of Child Abuse
and Neglect
1205 Oneida Street
Denver, CO 80220

National Child Abuse Coalition
(Child advocacy)
1125 15th Street, N.W.
Suite 300
Washington, DC 20005

National Center on Child Abuse
and Neglect
Children's Bureau
Administration for Children,
Youth and Families
U.S. Dept. of Health and Human
Services
P.O. Box 1182
Washington, DC 20013

National Committee for
Prevention of Child Abuse
332 South Michigan Avenue
Suite 1250
Chicago, IL 60604

Parents Anonymous
(self-help)
22336 Hawthorne Blvd.
Suite 208
Torrance, CA 90505

Parents United/Daughters
and Sons United
(sexual abuse, self-help)
P.O. Box 952
San Jose, CA 95108

Other National Organizations

The following national organizations can help identify written material and resources that are available on the subject of child care and child abuse.

American Academy of Pediatrics
P.O. Box 1034
Evanston, IL 60204

Association for Childhood
Education International
3615 Wisconsin Avenue, N.W.
Washington, DC 20016

Association for the Care of
Children's Health
3615 Wisconsin Avenue, N.W.
Washington, DC 20016

Child Care Support Center
Save the Children
1182 W. Peachtree Street, N.W.
Suite 209
Atlanta, GA 30309

Child Welfare League
67 Irving Place
New York, NY 10003

Children's Defense Fund
(child advocacy, Child Watch)
1420 New York Avenue, N.W.
Washington, DC 20036

Clearinghouse on Elementary
and Early Childhood
Education
University of Illinois at
Champaign-Urbana
College of Education
University of Illinois
Urbana, IL 61801

Coalition for Families
1346 Connecticut Avenue, N.W.
Suite 312
Washington, DC 20036

Council for Exceptional Children
1920 Association Drive
Reston, VA 22090

Family Outreach of America, Inc.
1329 7th Street
Corpus Christi, TX 78404

Family Resource Coalition
230 North Michigan Avenue
Suite 1625
Chicago, IL 60601

Family Service Association
of America
44 East 23rd Street
New York, NY 10010

National Center for Missing
and Exploited Children
1835 K Street, N.W.
Suite 700
Washington, DC 20006

High Scope Foundation
600 N. River Street
Ypsilanti, MI 48197

Military Family Resource Center
6501 Loisdale Court, Suite 900
Springfield, VA 22160

National Center for Clinical
Infant Programs
733 15th Street, N.W., Suite 912
Washington, DC 20005

National Association for the
Education of Young Children
1834 Connecticut Avenue, N.W.
Washington, DC 20009

National Black Child
Development Institute
1463 Rhode Island Avenue, N.W.
Washington, DC 20005

National Child Commission on
Resources for Youth, Inc.
605 Commonwealth Avenue
Boston, MA 02215

National Committee for Adoption
1346 Connecticut Avenue, N.W.
Suite 326
Washington, DC 20036

National Foster Parent
Association
P.O. Box 257
King George, VA 22485

National Council of Churches
473 Riverside Drive
New York, NY 10115

North American Council on
Adoptable Children
1346 Connecticut Avenue, N.W.
Suite 229
Washington, DC 20036

Parents Without Partners
7910 Woodmont Avenue
Bethesda, MD 20814

School-Age Child Care Project
Wellesley College Center for
Research on Women
Wellesley, MA 02181

Single Dad's Lifestyle
P.O. Box 4842
Scottsdale, AZ 85258

National Committee for Prevention of Child Abuse

Step Family Association of
America
900 Welch Road, Suite 400
Palo Alto, CA 94304

Superintendent of Documents
(child care publications)
U.S. Government Printing Office
Washington, DC 20402

U.S. Department of Health
and Human Services
Administration for Children,
Youth & Families
Children's Bureau
P.O. Box 1182
Washington, DC 20013

Appendix D: Tips to Prevent Child Molesting

The following tips are reprinted from "When Child Care Becomes Child Molesting" and are reprinted by permission from the July 1984 issue of *Good Housekeeping* © 1984 by the Hearst Corporation.

What to Look For

- Don't hesitate to thoroughly check out any kind of child care, even if it's being offered by someone you know.
- Check to see if a center or home is licensed, but remember, a license means only that the place has met certain physical requirements; it indicates little about the quality of the care or the background of the care givers. Private care givers may not need to be licensed; requirements vary from state to state (check with the the social-service or health department or with a child-care information and referral service).
- Talk to other parents who use the care giver or center you are considering. Ask a private care giver for references *and check them*. Also ask for the care giver's employment history, especially past jobs involving children. Ask a center whether it does thorough background checks on its employees and how they are done.
- Arrange to interview the care giver at the place where your child will be cared for and take your child with you. Make sure the care giver's views on discipline agree with yours.
- After the interview sit and watch how the care giver relates to your child and the other children she cares for. How is misbehavior handled? Does the care giver seem interested in the children or harassed? Do the children seem happy and busy or withdrawn and fearful?
- Find out how your child will be spending his or her time during the day. Is there a daily schedule? Too much idle time is a bad sign. Make sure there are enough toys, books, and other kinds of play equipment.
- Make sure the care giver understands he or she must ask permission to take your child off the premises for a shopping or field trip and that your child is never to leave with another adult unless you say so.
- Tour the home or center and make sure you see the entire area, inside and out. If you are kept away from a particular room or area, *don't use that care giver*.
- If you have decided on a care giver, arrange for a short trial period first.
- After you have arranged for care, drop into the home or center unannounced from time to time. Never use a care giver or center that does not allow unannounced visits.
- When you pick up your child at the end of the day, casually ask the care giver what went on that day. Also talk to your child about the day's activities. Keep in contact with parents of the other children.
- If your child seems unusually upset about being left at the home or center, find out why.

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7. Heinicke, et al. "The Organization of Day Care: Considerations to the Mental Health of Children and Family." *American Journal of Orthopsychiatry,* 43:1 8-22, Jan. 1973.

Other NCPCA Publications

The National Committee for Prevention of Child Abuse (NCPCA) distributes and publishes educational materials that deal with a variety of topics, including parenting, child abuse, and child abuse prevention. The NCPCA catalog is available free upon request from NCPCA, Publishing Dept., 332 S. Michigan Ave., Suite 1250, Chicago, IL 60604-4357, (312) 663-3520.

Written in a conversational style, the publications are excellent reading for professionals, lay persons, and students. Selected publications, as indicated, are available in Spanish. Some NCPCA titles are:

Child Abuse Prevention

Strengthening the Family through the Workplace
An Approach to Preventing Child Abuse
Healthy Preschoolers through Community Action
It Shouldn't Hurt to Be a Child
Evaluating Child Abuse Prevention Programs
Self-Help and the Treatment of Child Abuse
My Brother Got Here Early

Child Abuse

Emotional Maltreatment of Children
Physical Child Abuse
Understanding Sexual Child Abuse
Dealing with Sexual Child Abuse
Basic Facts about Sexual Child Abuse
Think You Know Something about Child Abuse? (English and Spanish)
Maltreatment of Adolescents
Physical Child Neglect

Parenting

What Every Parent Should Know (English and Spanish)
Child Discipline: Guidelines for Parents (English and Spanish)
Growth and Development through Parenting
Getting New Parents Off to a Good Start
Parent-Child Bonding: The Development of Intimacy (English and Spanish)
Foster Parenting Abused Children

Special Subjects

Child Abuse and the Law: A Legal Primer for Social Workers
Annotated Bibliography of Legal Articles on Child Abuse
The Disabled Child and Child Abuse
Catapulting Abusive Alcoholics to Successful Recovery

General Topics

Fund Raising in the Private Sector
Networking: What's It All About?

Mr. **Birch**. News stories have covered the cases of sexual maltreatment of children in day care programs, which are alarming. The statistical information we have, however, shows that child sexual abuse while growing nationally, only a very small percentage of that sexual maltreatment of children happens outside the family.

If the insurance industry is uneasy about the safety of children in day care, I would suggest looking to other corporations who've decided that in fact day care is good for business. According to a story in yesterday's Washington Post, 2,000 companies—which is triple the number 3 years ago—provide some kind of child care benefits to their employees. That's an endorsement.

Advocates for the prevention of child abuse, rather than pushing to close day care programs as a risk to children, are working to promote day care opportunities for more children. The National Child Abuse Coalition is anxious to work with you to combine our energies in a positive way to make sure that day care is safe for every child.

Thank you.

[Prepared statement of Thomas Birch follows:]

Prepared Statement of Thomas L. Birch, Legislative Counsel, National Child Abuse Coalition

Mr. Chairman, members of the Committee, my name is Thomas Birch. I am the legislative counsel for the National Child Abuse Coalition, an advocacy group composed of national organizations concerned about the future of services for the prevention and treatment of child abuse and neglect.

I want to thank the Select Committee for the opportunity to present testimony on the subject of the abuse of children in child care programs.

For well over a year now recurring news stories about the sexual abuse of children in day care programs have shocked the nation, frightened parents, and lately, as this Committee has heard, convinced insurers into believing that children in this country put in child care programs by their parents are in grave danger of being molested.

The fact is, information on reported child molestation refutes the presumption that children in day care are at high risk of sexual abuse. The data we have do not support that notion. What's more, advocates for the prevention of child abuse see day care as an importnat effort to help prevent the abuse of children, the reason why citizens in communities across the country are actively working to make sure that children in day care are not in danger.

NUMBERS OF CHILDREN ABUSED

Child abuse and neglect is a national problem of huge proportions. Over a million documented cases are reported in the United States each year. This Committee is well aware of the tremendous yearly increases in reports of child abuse. According to the American Humane Association [AHA], which compiles annually national child abuse and neglect reporting statistics, the number of children reported to child protective service agencies increased by 121 percent from 1976 to 1983.

AHA in its 1983 survey, the year for which the most recent information has been compiled, reported 1,007,658 documented cases of child abuse and neglect, an increase of 8.4 percent over the previous year.

Another survey conducted early this year by the National Committee for Prevention of Child Abuse [NCPCA] estimated that for 1984 reports rose again by 19 percent to 1,273,000 children abused and neglected.

The number of children included in these reports who have been sexually abused has increased each year at a greater rate—up by 23 percent in 1983 according to American Humane, and an increase of 35 percent last year reported by the National Committee.

This is not an appealing story, but what does it mean about the risk of children being sexually abused in day care programs?

AHA tells us that in 1983 child sexual maltreatment accounted for 8.5% of reported cases of child abuse and nelgect—that is, of the 1,007,000 documented reports of all types of child abuse and neglect slightly more than 8,500 children were sexually maltreated that year.

According to the information we have, most of those children were sexually abused in their own homes by their parents. The statistics show that in 97.1 percent of the cases I have mentioned a parent or some other relative is the sexual molester. The remaining 3 percent of the perpetrators includes babysitters, teachers, neighbors, strangers, parents' friends, and the staff of state and private institutions.

American Humane estimates that between one and one and a half percent of the reported perpetrators of child sexual abuse fall into the category of daycare employees.

In addition when we look further at the statistics we discover that day care employees as a group would be expected to have fewer child sexual abusers among their ranks than the general population. The reason is simple. Surveys estimate between 78 and 92 percent of child sexual abusers are male while approximately 95 percent of child care workers are female.

This statistical information should help, I think, to put into perspective the problem of sexual abuse of children in day care programs, a problem much enlarged in the public's mind by the news coverage given to cases that have occurred. The data enforce the belief that child sexual molestation is increaseing in this country but that sexual maltreatment of children by day care workers is a very small piece of the problem.

CHILD CARE AS PREVENTION

As I have said, those who are working to prevent child abuse believe that child care is an integral part of that effort by helping to strengthen families. In fact, in most subsidized child care, abused and neglected children have first priority for service.

Good child care services can fill many of the goals of a child abuse prevention program: enhancing ties and communication between parents and children, increasing parents' skills in coping with the stresses of caring for their children, reducing family isolation, increasing peer support and improving access to social and health services for the family. Without optimal child care services, the risk of child abuse increases.

Most child abuse occurs in families under stress. Research has suggested that the availability of day care helps alleviate that stress and increases family well-being. The rising numbers of families with both parents or with single parents in the work force brings with it a rise in the level of stress facing working parents and their children. Child care is a necessary support for these families.

Knowing their children are safe and well cared for can give parents the assurance needed to relieve their worry while at work or away from home. Without that assurance and time away from child care responsibilities, parents can become tense and less able to cope with the pressures of rearing their children.

Isolation is a factor affecting a family which often contributes to child abuse. A child care center teacher or other parents with children in the program can offer some relief to a parent who feels isolated.

Day care center teachers can also help parents learn better how to care for their own children. Parents who have abused their children or may be liable to abuse often have unrealistic expectations of their children's capabilities. Day care teachers can help mothers and fathers understand a child's normal behavior, and show parents how to cope with raising children.

Crisis care is an important special child care program that is crucial for preventing child abuse. Parents who feel enormous pressure can bring their children to a crisis nursery for several hours or several days. The time away from the demands of a child can give a parent the chance to relax and prevent a parent from venting frustrations on a child.

Disabled children, whose special needs place unusual demands upon parents often unprepared to cope with the new burdens, are children at high risk of being abused. Child care can be important to the prevention of such abuse. Child care services for handicapped youngsters can be of enormous benefit in providing the developmental needs of disabled children while assisting and educating parents in their responsibilities to their children. Respite child care offers the parent of a disabled child a few hours of relief and can be an excellent approach to preventing the abuse that extra burden of care might cause.

Day care has another role to play in preventing child abuse and in treating children who have been abused. Child care programs employ therapists to work with abused children—and have have been especially effective with children who were sexually abused, to help relieve the anxiety and fear they experience from having been abused, and to develop improved self-esteem in the youngsters. Because prevention of further abuse should be a major goal of therapeutic child care, parents are involved in the program too, receiving counseling and participating in the program's activities with their children.

PREVENTING SEXUAL ABUSE IN CHILD CARE

Because day care is so important, not only as a part of the effort to prevent child abuse, but as a basic service required by the families of millions of children across the country, day care providers, public officials—including the Chairman and members of this Committee—and child abuse prevention advocates have joined forces to ease the minds of parents with children in day care and to protect those children by preventing the abuse and sexual molestation of children in day care from ever having the chance to happen.

Indeed child abuse prevention advocates are now exercising the same kind of creative response used to prevent family sexual abuse to stopping the out-of-home sexual abuse of children.

The most effective method of preventing the molestation of children is to educate parents, children, teachers, and day care staff to recognize, to resist and to report sexual abuse.

Here are some of the steps being taken to make sure day care is safe for children.

With the passage last year of P.L. 98-473, legislation authored by Chairman Miller provided $25 million to states for child sexual abuse prevention training. A recent report of the National Association of Public Child Welfare Administrators showed 46 states responding to a survey plan to provide training in sexual abuse prevention.

The new law, as you well know, also requires states to set up criminal record and background checks on day care employees. Prior to the federal mandate only three states had comparable laws, but since last year over half have enacted or are contemplating such legislation.

From the federal Department of Health and Human Services (HHS) the Inspector General in a January 1985 report on preventing sexual abuse in day care programs recommended that, as a first priority, HHS should support the kinds of education programs I have described, which is why we were disappointed when the Administration's fiscal 1986 budget proposed eliminating the $25 million to states for sexual abuse prevention training. We have been encouraged by your leadership Mr. Chairman, joined by your colleagues on this Committee and others in the House, to make sure that Congress provides this much needed support for another year.

The National Center on Child Abuse and Neglect [NCCAN], which is the federal agency charged with addressing the prevention and treatment of child abuse, has, among other activities, published a pamphlet made widely available on tips for parents on how to prevent child sexual abuse and how to shop for a day care program. It suggests, for example, making sure that parents can drop in for a visit at the day care program at any time and the parents are informed about every outing planned for their children.

Scores of films, books, school curricula, plays and brochures have been developed by local organizations to teach parents and children about preventing sexual abuse. These are not sex education programs, they offer public health and safety education.

The Kansas Committee for Prevention of Child Abuse has produced a play, "Bubbylonian Encounter", presented all over the country in live performances and on videotape to young school children to teach them about different kinds of touching.

The San Francisco Child Abuse Council has developed a school curriculum that educates teachers, principals, parents and children about child sexual abuse. The Committee for Children in Seattle, Washington has a personal safety curriculum called "Talking About Touching with Preschoolers."

In an effort that has reached hundreds of thousands of families, the National Committee for Prevention of Child Abuse has collaborated with Marvel Comics to produce a special Spiderman comic book showing children how to protect themselves from sexual molestation.

Parents Anonymous, a national voluntary self-help organization, has initiated community sexual abuse prevention forums, beginning in Southern California, for parents who wish to learn more about protecting their children from sexual abuse and how best to identify good, safe preschool programs.

CONCLUSION

News stories have covered cases of the sexual maltreatment of children in day care programs which are alarming. The statistical information we have shows that child sexual abuse is a growing problem nationally but that only a very small percentage of the sexual maltreatment of children happens outside the family.

If the insurance industry is uneasy about the safety of children in day care I would suggest looking to other corporations which have decided that day care is good for business. In 1982 the National Employer Supported Child Care Program surveyed 415 companies that provide some kind of child care assistance to their employees. Corporations like John Hancock make donations to nonprofit child care centers in the community. Polaroid provides employees with vouchers to pay for day care. Other companies, like Stride Rite, offer on-site child care centers.

Advocates for the prevention of child abuse rather than pushing to close day care programs as a risk to children are working to promote day care opportunities for more children. The National Child Abuse Coalition is anxious to work with you, to combine our energies in a positive way to make sure that day care is safe for every child.

Chairman MILLER. Thank you. I would hope, Tom, that you would forward your statistics from American Humane to the insurance companies so that they can start to look at the actual numbers and the real potential for risk exposure. I don't expect them to accept them at face value, but I think they will start to reduce the level of trauma and the level of heat that has been generated around this subject, and start to shine some light on it. I think, once again, what we're seeing is that we were given to believe there was a national epidemic of child abuse and sexual molestation in child care centers throughout the entire country, and what in fact we had was the repeat of allegations and the repeat of a few stories over and over again.

That's not to suggest that it's not a problem but it is to suggest that it is not in the magnitude that justifies what the insurance industry's response to those stories are. We are left with the evidence that what they did is respond to a series of newspaper and media reports, and they made a decision based upon that.

What you are suggesting in your testimony is that may not be the real story or the actual facts with respect to the national problem that concerns all of us. I would hate to think the insurance industry used those stories to conveniently get out of this coverage. I mean that would be the height of cynicism and I'm not prepared to go that far yet. But again, I think what we're seeing is that we have people responding in an emotionally charged atmosphere, and responding without the full benefit of the facts.

I think we're starting to see this with respect to missing children. When we start to break down the numbers of children who were taken and abducted by a stranger, we find out that it's far far less than anybody has discussed in this country in the last year. And I think when we talk about the actual cases of abuse and the potential for abuse in child care and day care centers and family day care homes, it turns out to be far less than the immediate hysteria of the last 12 to 18 months. I would hope that the insurance companies would come to you and start working with those facts to see exactly how they can justify their policies.

Mr. BIRCH. Well, I appreciate your suggestion. The news is obviously a powerful force in generating public emotions and that's certainly what's happened in this case. It strikes me as a little surprising that an industry which I believe prides itself on actuarial figures and data appears to have made decisions regarding the insurability of day care programs without looking at any of this information which is available.

Chairman **Miller**. Maybe we can start in Connecticut. Representative Nystrom, I don't know how you're going to proceed. There's two things that I think that have been raised here. One concerning the actual evidence in terms of the incidence of abuse in the child care setting, and the other one clearly is, and I think properly so, that the industry is saying we're a little concerned about the haphazard nature of the child care industry. I think that's shared by a lot of people, both inside the insurance industry and out.

And I just wondered to what extent state regulation is entering into the discussions at the Connecticut level?

Mr. **Nystrom**. Well, in Connecticut, the regulations differ. Some of that's due to the responsibility of more than one agency that does the licensing for day care. Perhaps that's an error in Connecticut and we are looking and have been addressing the fact of consolidation of services at some point.

However, I think it's clear that the insurance industry does not have the accurate data to justify what is happening to those who provide day care services, and we in Connecticut are looking at that. We do feel that the rates should take accurate data into account. They should also take into account the types of services that are provided at particular day care centers. In Connecticut, you have three types of day care. There's family day care which is a number of children, you are limited one to six. The next group goes up 6 to 12, and then up 12 and above. At the 12 and above status, it's a center. When you get to the center aspect, you have greater needs that have to be met. They are defined by statute in Connecticut.

Consequently, I would assume that the insurance industry should, if they are not doing so, consider different ratings depending on the types of service that are offered at a particular day care center.

Chairman **Miller**. Well, as one of your legislators from Connecticut reminded me last night, when you talk about insurance, people think about Connecticut, so maybe there's an opportunity there in terms of your work with the industry in leading us out of this morass. And I would hope that you would bring back there some of the evidence from the National Child Abuse Coalition, so that we can start to rationalize some of the decisions that have been made.

I want to thank you very much for your testimony and for your contributions to this morning's hearing. As I indicated earlier in the hearings, I would hope that this matter would be sorted out in a rather expeditious fashion, because if it's not, I think it's very clear that we're going to have to find someway to respond. We're simply not going to do without a child care industry in this country. That's just totally unacceptable.

We cannot take those parents out of the economic loop. As a Government, we don't want to pay for the assistance to those families if they have an opportunity to provide for their own well-being, so that result is unacceptable.

And I think it's clear in my discussions with other committees that have far more jurisdiction over this industry than we do that this concern is shared, and to the extent we have to seek Federal resources for improperly excessive premiums, it's going to be a problem for Congress.

I want to thank you for your contributions. The committee will stand in recess on this subject, and we wait to have additional evidence brought forth to us by the companies. Thank you very much.

[Whereupon, at 1:30 p.m., the select committee was adjourned, subject to the call of the Chair.]

[Material submitted for inclusion in the record:]

NEW YORK STATE CHILD CARE COORDINATING COUNCIL

54 Washington Street, Hempstead, NY 11550
(516) 538-1362

Statement for the Record of the Public Hearing of
Select Committee on Children, Youth and Families
U.S. House of Representatives
July 18, 1985
on
Child Care: The Emerging Insurance Crisis

The New York State Child Care Coordinating Council and its affiliates, the county day care/child development councils, have become aware of serious problems in liability insurance coverage for child day care providers and affilated services in New York State. The State Council has initiated a survey of the 940 day care centers licensed by the New York State Department of Social Services in cooperation with the New York State Insurance Department and will survey family day care providers through its affiliates.

Some of the problems that have surfaced to date include:

- Dramatic increase in liability insurance rate for day care centers with a "clean" claims record, and at the same time cancellation of some coverage (Dutchess County);
- Cancellation of all liability insurance, including bus insurance, for a proprietary center which has had no claim of any kind (Rockland County);
- Cancellation of liability insurance coverage for child abuse/sexual abuse (Dutchess County);
- Exorbitant fee for liability insurance for a new day care center ($7,000/yr. for 30 children -- Onondaga County);

Local Affiliates in

Counties of
  Albany
  Allegheny
  Broome
  Cayuga
  Chautauqua
  Chemung
  Columbia
  Cortland
  Delaware
  Dutchess
  Erie
  Genesee
  Jefferson
  Livingston
  Madison
  Monroe
  Nassau
  Oneida
  Onondaga
  Ontario
  Orange
  Orleans
  Oswego
  Otsego
  Putnam
  Rensselaer
  Rockland
  St. Lawrence
  Schenectady
  Schoharie
  Seneca
  Steuben
  Suffolk
  Sullivan
  Tompkins
  Ulster
  Wayne
  Westchester
  Wyoming
  Yates
City of New York

The New York State Child Care Coordinating Council, Inc., is a not-for-profit organization which provides technical assistance, information, and advocacy services to its affiliates, the county day care/child development councils. Other organizations with a common concern may become members, as well as interested individuals.

- Cancellation of Homeowners Insurance for family day care providers covered by liability insurance through the county department of social services (Tompkins County);
- Cancellation of liability insurance for licensed family day care providers with no claims record (Rockland County);
- Lower levels of coverage for Child Care Resource and Referral Services, including exclusion of bodily harm (Day Care Council of Nassau).

The location cited in each case is the first instance to come to our attention.

The Human Resources Administration of the City of New York in January 1985 was able to develop coverage for the 340 day care centers it funds, for the City's 90 Head Start Centers, and for its 2,000 family day care providers. We have yet to determine the insurance status of the 400 private centers in the City of New York, licensed by the Bureau of Day Care of the City's Health Department.

Another group of providers which appears to have little or no problem is composed of multi-service agencies which provide child day care services as one of a wide range of services to children and families. These multi-service agencies range in size from Family of Woodstock in Ulster County to the Catholic Diocese of New York covering Manhattan and a number of counties to the north.

When the New York State Child Care Coordinating Council has completed its surveys in conjunction with the New York State Insurance Department and with its affiliates, the results will be forwarded to the Select Committee. We are most appreciative of your interest in this critical issue affecting services to children and families.

DOL 7-17-85

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TELEPHONE 226-7660

U.S. House of Representatives
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WASHINGTON, DC 20515

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MARK SOUDER
MINORITY STAFF DIRECTOR

TELEPHONE 226-7692

July 16, 1985

Bruce Bunner
State Insurance Commissioner
California Department of Insurance
700 L Street
Sacramento, California 95814

Dear Commissioner Bunner:

The Select Committee on Children, Youth, and Families will be holding a hearing on "Child Care: The Emerging Insurance Crisis" on July 18, 1985. The purpose of the hearing is to investigate recent reports of increasing numbers of child care providers who are experiencing loss of their liability insurance.

Since you have indicated that you are unable to testify at the hearing, I would like to invite you to submit a statement to the Select Committee in your capacity as the California State Insurance Commissioner.

Reports have come to us from child care centers, family day care homes, Head Start programs, and resource and referral agencies that their liability policies are not being renewed, that premiums have become prohibitive, that coverage for child abuse claims is unavailable, and that policies are being cancelled with little or no notification.

The problem is complicated in California, where legislation was recently passed which requires child care programs to carry specific levels of liability insurance.

In order to investigate the justification for these changes in policy toward the child care industry, we would appreciate it very much if you would address the following questions:

1. Has the state Department of Insurance determined that there is a sound actuarial basis for the modifications in policy by conducting a thorough review and analysis of these changes? If so, please forward to us the dates and records of any hearings held on this issue.

   Has the Department of Insurance approved rate increases or terminations of policies for child care programs (centers, family day care homes, Head Start programs, resource and referral agencies)? If so, please forward the notification of such approval. If not, do you intend to review them?

2. How many child care related claims have been made in California during the last three years and what have such claims been based on?

   How much has been paid in premiums by child care programs for the last three years?

   For each of the last three years, how much money has the industry paid out in child care related claims? How much for child abuse in child care; for accidents in child care; other claims (list by type of claim)?

3. Is there additional information that substantiates actual losses by the insurance industry in California due to coverage of child care providers?

4. If many policies currently exclude or will soon exclude coverage for child abuse claims, what would be the rationale for cancellation or excessive rate hikes at this time?

The record of the hearing will be held open through Thursday, August 1. Please forward your statement to: Rm. H2-385, House Annex 2, Washington, D.C., 20515, Attn: Ann Rosewater. Should you need further information or assistance, call Ann Rosewater at the Select Committtee office, (202) 226-7660.

Thank you for assisting the Select Committee in its efforts.

Sincerely,

George Miller

GEORGE MILLER
Chairman,
Select Committee on Children,
  Youth, and Families

STATE OF CALIFORNIA
GEORGE DEUKMEJIAN, Governor
DEPARTMENT OF INSURANCE
600 SOUTH COMMONWEALTH AVENUE
LOS ANGELES, CALIFORNIA 90005

July 31, 1985

The Honorable George Miller
U. S. House of Representatives
Select Committee on Children, Youth & Families
Rm. H2-385 House Annex 2
Washington, D.C. 20515

Dear Mr. Miller:

This is in response to your July 1, 1985 letter concerning the child care liability insurance problem.

For your convenience, I have repeated the questions in the same order as posed in your letter.

1(a)Q: Has the State Department of Insurance determined that there is a sound actuarial basis for the modifications in the policy by conducting a thorough review and analysis of these changes? If so, please forward to us the dates and records of any hearings held on this issue.

A: No. We have not made such determination nor have we held a hearing on this issue. In the State of California, the child care provider liability insurance is subject to the open competition rating law, also known as the McBride-Grunsky Insurance Regulatory Act of 1947. Under this statute the carriers are not required to file their rates, rating plan or policy forms for the Commissioner's approval.

(b)Q: Has the Department of Insurance approved rate increase or terminations of policies for child care programs (Centers, family day care homes, head start programs, resource and referral agencies)? If so, please forward the notification of such approval. If not, do you intend to review them?

A: No. We neither approve nor disapprove a company's actions for the same reason as stated above. We may initiate a special underwriting and rating examination if the source of the problem is coming from the carriers' underwriting and rating practice. However, we do not believe that such an examination would solve the problem. We perceive that the real problem comes from a tight insurance market and adverse publicity in some child abuse cases. This has caused some availability problems in the marketplace for this type of insurance.

2(a)Q: How many child care related claims have been made in California during the last three years and what have such claims been based on?

A: My staff has contacted the Insurance Services Office (ISO) for such data. According to ISO information, there was a total of 1,131 claims filed in the nation against the insurers for the policy years 1980 through 1983. For California, there was a total of 215 claims for the same policy years. The attached Exhibit, Table 1 shows the nationwide figures and Table 2 shows the California figures. The data reflects only those companies who were reporting their statistics to ISO.

(b)Q: How much has been paid in premium by child care programs for the last three years?

A: According to ISO data, the nationwide earned premium for policy years 1980 through 1983 was approximately $12 million. For California, the earned premium was approximately $2.5 million. (See the attached exhibit for details)

(c)Q: For each of the last three years, how much money has the industry paid out in child care related claims? How much for child abuse in child care; for accidents in child care; other claims (listed by type of claim)?

A: The child care liability incurred losses are broken down by Basic Limit Bodily Injury claims ($25,000 is the basic limit), Excess Limit Bodily Injury claims, and medical payment. According to ISO data, during policy years 1980 through 1983, the companies' nationwide total incurred losses is over $7 million for basic BI claims, about $5 million for excess BI claims, and $293,000 for medical payment. For California, the incurred losses are approximately $1.2 million for basic BI claims, $324,000 for excess limit BI claims, and $67,000 for medical payment claims. (See Exhibit) With respect to your question on how much has been paid out for child abuse claims or accident claims, the ISO statistical plan does not provide a coding for the cause of loss detail; therefore, no such data are available.

3 Q: Is there additional information that substantiates actual losses by the insurance industry in California due to coverage of child care providers?

A: No.

4 Q: If many policies currently exclude or will soon exclude coverage for child abuse claims, what would be the rationale for cancellation or excessive rate hikes at this time?

A: The insurance industry as a whole has just gone through an adverse underwriting cycle. Carriers are striving to improve their underwriting results. Due to widespread adverse publicity in some child abuse cases, the underwriters are concerned that exorbitant litigation costs may impair the company's underwriting profitability. Therefore, they are exercising their underwriting judgment to eliminate what is perceived as undesirable business from their book of business.

Under the California statute, there are no laws restricting an insurance company from cancelling or non-renewing a commercial insurance policy. In rare cases, the day-care provider may be insured under a regular homeowner policy. In this instance, the non-renewal or cancellation is somewhat restricted. Carriers choosing to do so must comply with the provisions set forth in California Insurance Code Sections 675-679.

With respect to your question as to what would be the rationale for excessive rate hikes at this time, I must clarify the term "excessive" before answering your question. California Insurance Code Section 1852(a) defines the standard of excessiveness as follows: "No rate shall be held to be excessive unless (1) such rate is unreasonably high for the insurance provided and (2) a reasonable degree of competition does not exist in the area with respect to the classification to which such rate is applicable."

Basically, during the soft market period, companies did not price the coverage at its correct rate level. Now the companies are adjusting the rates to such a level that it would generate sufficient premium to cover the losses and business expenses allowances. Of course, these adjustments need no prior approval from the Department of Insurance under California Rating Laws provided that they meet the general standards as set forth in California Insurance Code Section 1852(a).

In our opinion, the main problem is not whether carriers can justify the rate increase. According to the statistics provided by Insurance Services Office, I believe that most carriers probably can reasonably justify the rate increases. The real problem is that many carriers simply do not wish to offer this type of coverage, and never provided a market for it. There is nothing in the California statutes that would give the Insurance Commissioner the authority to mandate that insurance companies must provide specific coverages. A possible alternative solution is for the California legislature to provide authority to the Department of Insurance to form a pool or so-called Joint Underwriting Association for the purposes of insuring day-care providers if it appears that the availability of this coverage is a problem in this state.

Sincerely yours,

BRUCE BUNNER
Insurance Commissioner

BB:bm
Attachments

EXHIBIT

CHILD CARE LIABILITY INSURANCE

LOSS EXPERIENCE

TABLE 1

COUNTRYWIDE

Policy Year	(1) Earned Premium	(2) BI/Basic Limit* Incurred Losses	(3) BI/Excess Limit Incurred Losses	(4) Medical Payment	(5) No. of Claim	(6) Losses & LAE Ratio**
12/31/80	$1,785,529	$ 983,150	$ 243,127	$ 39,779	178	0.709
12/31/81	2,581,645	1,144,240	997,137	44,807	205	0.847
12/31/82	3,321,139	2,041,498	1,340,296	89,347	321	1.045
12/31/83	3,995,362	2,864,361	2,332,868	119,021	427	1.331
TOTAL	$11,683,675	$7,033,249	$4,913,428	$ 292,954	1131	1.048

****

TABLE 2

CALIFORNIA

Policy Year	(1) Earned Premium	(2) BI/Basic Limit Incurred Loss	(3) Excess Incurred Loss	(4) Medical Payment	(5) No. of Claim	(6) Loss & LAE Ratio
1980	443,280	157,094	0	10,161	31	0.377
1981	610,784	232,590	61,703	11,359	49	0.500
1982	689,602	267,300	120,048	23,787	59	0.596
1983	738,480	560,361	142,680	21,945	76	0.982
TOTAL	2,482,146	1,217,345	324,431	67,252	215	0.648

Note: *1. The basic limit is $25,000. The incrred losses include loss adjustment expenses (LAE)
**2. Column (6) is the sum of columns (2), (3) & (4) divided by column (1)
3. Data are provided by Insurance Services Office (ISO)

BMF
MARKETING California

IMPORTANT NOTICE

ADVERSE PUBLICITY IN THE CARE INDUSTRY HAS BEEN SCARING INSURANCE COMPANIES THROUGHOUT THE COUNTRY. MANY COMPANIES WHO HAVE BEEN WRITING THE INSURANCE HAVE BEEN DISCONTINUING THE PROGRAMS OR CHARGING RATES FOUR AND FIVE TIMES MORE THAN OUR CURRENT RATES.

MISSION INSURANCE IS ONE OF THOSE COMPANIES TO DISCONTINUE OFFERING COVERAGE FOR THE CARE PROVIDER INDUSTRY AFTER JUNE 30, 1985.

WE ARE ATTEMPTING TO FIND A NEW COMPANY TO REPLACE THE MISSION INSURANCE FOR OUR NATIONWIDE PROGRAM PRIOR TO THIS DATE.

HOWEVER, IF THE MISSION INSURANCE COMPANY DECIDES TO CANCEL THIS POLICY BEFORE THE END OF YOUR POLICY PERIOD, THEY MUST FIRST GIVE YOU 60 DAYS WRITTEN NOTICE OF CANCELLATION. AFTER ANY COMPANY CANCELLATION, THEY MUST RETURN YOUR UNUSUED PREMIUM.

WE WILL CONTINUE TO KEEP YOU AND YOUR ASSOCIATION NOTIFIED OF ANY FUTURE DEVELOPMENTS OR CHANGES. WE WISH TO THANK YOU FOR YOUR ASSISTANCE AND COOPERATION.

CUSTOMER SERVICE DEPARTMENT

BMFM 3/15/85

15250 Ventura Blvd., Ste. 1012 / Sherman Oaks, CA 91403-3288 / (818) 905-0311 / (800) 624-0912 / Out of State (800) 423-8733
BMF MARKETING INSURANCE SERVICES, INC., a Bayly, Martin & Fay International Company

KIND OF POLICY: FAMILY DAY CARE PROVIDER POLICY

POLICY NO.: DCI 100 6467

CANCELLATION OR TERMINATION WILL TAKE EFFECT AT:

7-1-85 (DATE) 12:01 AM (HOUR-STANDARD TIME)

DATE OF MAILING: 6-24-85

ISSUED THROUGH AGENCY OR OFFICE AT:

BMF MARKETING INSURANCE
SERVICES, INC.
SHERMAN OAKS, CA. 91403

INSURANCE COMPANY:

MISSION INSURANCE COMPANY
P.O. BOX 2121
GLENDALE, CA. 91209-2121

NAME AND ADDRESS OF INSURED:

SOLON, KAREN E.
7441 MASON LANE
FALLS CHURCH, VA. 22042

Applicable item marked ☒

CANCELLATION

☐ You are hereby notified in accordance with the terms and conditions of the above mentioned policy that your insurance will cease at and from the hour and date mentioned above.
If the premium has been paid, premium adjustment will be made as soon as practicable after cancellation becomes effective.
If the premium has not been paid, a bill for the premium earned to the time of cancellation will be forwarded in due course.

☐ You are hereby notified in accordance with the terms and conditions of the above mentioned policy that your insurance will cease at and from the hour and date mentioned above due to nonpayment of premium.
A bill for the premium earned to the time of cancellation will be forwarded in due course.

☐ You are hereby notified in accordance with the terms and conditions of the above mentioned policy, and in accordance with law, that your insurance will cease at and from the hour and date mentioned above.
If the premium has been paid, premium adjustment will be made as soon as practicable after cancellation becomes effective.
If the premium has not been paid, a bill for the premium earned to the time of cancellation will be forwarded in due course.

☐ Reason for cancellation: Nonpayment of premium.

Reason(s) for cancellation (other than for nonpayment of premium): ______

See the "Important Notices" section below for Additional Information Regarding the Reason(s) for Cancellation.

NONRENEWAL

☒ You are hereby notified in accordance with the terms and conditions of the above mentioned policy that the above mentioned policy will expire effective at and from the hour and date mentioned above and the policy will NOT be renewed.

☐ You are hereby notified in accordance with the terms and conditions of the above mentioned policy, and in accordance with law, that the above mentioned policy will expire effective at and from the hour and date mentioned above and the policy will NOT be renewed.

Reason(s) for nonrenewal: ______

See the "Important Notices" section below for Additional Information Regarding the Reason(s) for Nonrenewal.

IMPORTANT NOTICES

Additional Information Regarding the Reason(s) for Cancellation/Nonrenewal: You have the right to know the specific items of information that support the reasons given for this decision and the identity of the source of that information. You also have the right to see and obtain copies of documents relating to this decision.

If you ask us to correct, amend, or delete any information about you in our files and if we refuse to do so, you have the right to give us a concise statement of what you believe is the correct information. We will put your statement in our file so that anyone reviewing your file will see it.

If you would like additional information concerning this action, state law requires that you submit a written request within ninety (90) business days of the date this notice was mailed to you. Please send your request to:

(Name and address of the person or department to contact for additional information)

☐ Consumer Report: In compliance with the Fair Credit Reporting Act (Public Law 91-508), you are hereby informed that the action taken above is being taken wholly or partly because of information contained in a consumer report from the following consumer reporting agency:

(NAME)

(ADDRESS)

Authorized Representative

[illegible] (Ed. 10-83) © [illegible]

INSURED'S COPY

KIND OF POLICY

	ISSUED THROUGH AGENCY OR OFFICE AT:	CANCELLATION OR TERMINATION WILL TAKE EFFECT AT: (DATE)	(HOUR—STANDARD TIME)	DATE OF NOTICE
.00 82 39	BMF MARKETING INSURANCE SERVICE SHERMAN OAKS, CA 91403	9-2-85	12:01 A.M.	7-1-85

MISSION INSURANCE COMPANY
P.O. BOX 2121
GLENDALE, CA 91209-9990

CHESSNOE, ALYCE
9701 GLENWAY COURT
BURKE, VA 22015

(Applicable item marked ☒)

☒ You are hereby notified in accordance with the terms and conditions of the above mentioned policy that your insurance will cease at and from the hour and date mentioned above. REASON: PROGRAM DISCONTINUED.

If the premium has been paid, premium adjustment will be made as soon as practicable after cancellation becomes effective.

If the premium has not been paid, a bill for the premium earned to the time of cancellation will be forwarded in due course.

☐ You are hereby notified in accordance with the terms and conditions of the above mentioned policy that your insurance will cease at and from the hour and date mentioned above due to nonpayment of premium.

A bill for the premium earned to the time of cancellation will be forwarded in due course.

☐ You are hereby notified in accordance with the terms and conditions of the above mentioned policy that the above mentioned policy will expire effective at and from the hour and date mentioned above and the policy will NOT be renewed.

☐ In compliance with the Fair Credit Reporting Act (Public Law 91-508), you are hereby informed that the action taken above is being taken wholly or partly because of information contained in a consumer report from the following consumer reporting agency:

(NAME)

(ADDRESS)

Authorized Representative

3-73) © [illegible]

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